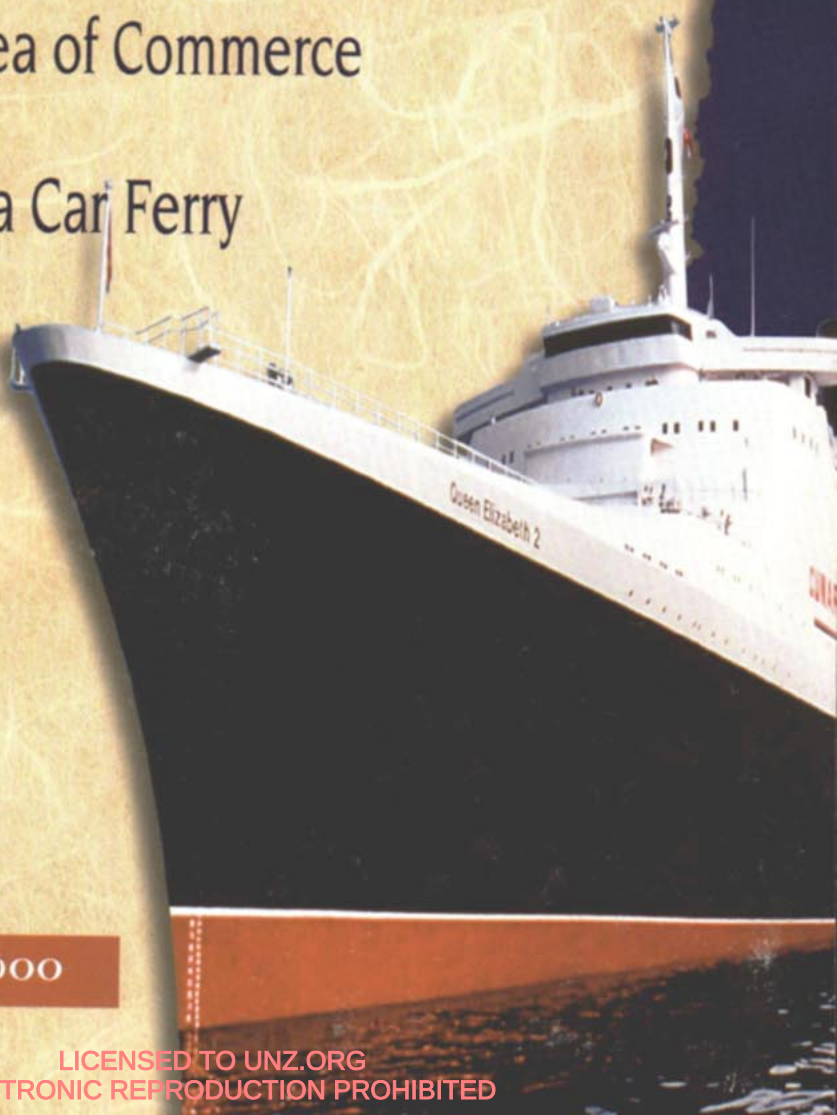


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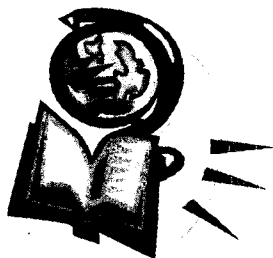
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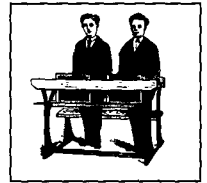
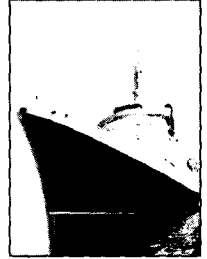
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Cover photo of the OE2 courtesy of Cunard Lines.

PERSPECTIVE

Double Take

By now you've noticed that *The Freeman: Ideas on Liberty* has become simply *Ideas on Liberty*. We made the change for several reasons, the major one being the unfortunate association of the name with a group with which we in fact are not associated.

Ideas on Liberty has as intimate a connection with the Foundation for Economic Education as *The Freeman*. It was the name of FEE's first periodical. When FEE founder and president Leonard Read brought *The Freeman* to FEE in 1956, he merged the two publications and made *Ideas on Liberty* the subtitle for the new magazine. Those words have been on the cover ever since. Rather than a name change, then, it is more a refinement. After all, what words better describe this magazine than *Ideas on Liberty*? That is what it has always been about. And that it will remain.

We strove to maintain the magazine's appearance despite the change in title. That's our way of saying that the content will continue to be the best writing on individual freedom, private property, the market order, and the rule of law to be found anywhere.

We see *Ideas on Liberty* as Leonard Read saw it: as part of the lifelong endeavor to understand liberty in all its fullness. As Read wrote in the first issue of *Ideas on Liberty* in 1955,

[L]iberty, like truth, is an object of infinite pursuit, a quest without end, ever! . . . In brief, not a single person among us is justified in regarding himself other than as a student of liberty. No know-it-all exists or ever will.

In searching for a student of liberty, the search must be within one's self. In the world of persons, it is only within each of us that the fertile, explorable areas exist. The best explorer of oneself is oneself. It is not possible to impart to others that which we do not possess. And even after we have made some progress in understanding, the most we can do for others is to make known to them a willingness to share what we have discovered by our own thinking, or

what we find edifying from recorded thinking. Whether or not what we offer is, in fact, shared, is beyond our power; and we should realize this.

* * *

The story of the transatlantic ocean liner is one of bold entrepreneurship and technological innovation. It's also a story of international competition, triumph, and tragedy. Anthony Young has the details on this titanic episode in the history of private enterprise.

On a smaller scale, car ferries have also succeeded in providing valued consumer services when left to private enterprise. But politicians never seem to get the message, as Andrew Morriss points out.

Everyone who studies economics begins with the supply-and-demand diagram, which purports to illustrate how market-clearing prices are determined. Yet there is something strangely dissatisfying about it as presented by mainstream economics. As Israel Kirzner shows us, that dissatisfaction is justified.

Crime has been diminishing, and every politician has been scrambling to grab some of the credit. Bruce Benson suggests, however, that much of the praise should go to the private citizens who take crime prevention into their own hands.

A key to a better life is technology, but it has certain prerequisites. Edward Younkens discusses the nature, requirements, and value of technology, and warns that government attempts to promote it are wrong-headed.

William Rappard was a Swiss classical liberal who left a large number of books explor-

ing the free society and the conditions necessary for world peace and commerce. Richard Ebeling chronicles the life of one of the century's most eloquent defenders of civil society.

The idea that everyone is equally qualified for education has been the foundation of government school systems for many years. It's an assumption that Albert Jay Nock eloquently challenged throughout his career as a defender of freedom and individualism. Wendy McElroy explores Nock's thoughts on education.

Our columnists have come up with provocative subjects this month: Donald Boudreaux draws two big lessons from the twentieth century. Lawrence Reed pays tribute to the politically shunned jitney. Doug Bandow debunks foreign aid. Thomas Szasz reveals the purpose of psychiatry. Dwight Lee shows why we shouldn't want to create jobs. Mark Skousen looks to the economics of the next century. Walter Williams ponders who benefits most from capitalism. And Roger Garrison says to those who believe that government stabilizes the economy: "It Just Ain't So!"

Our reviewers give the low-down on books about the enemies of science, Social Security reform, rising living standards, a forgotten antifederalist writer, the nature of economic theory, and the rule of law.

Finally, a correction regarding our November 1999 issue. In Wendy McElroy's article, "Is the Constitution Antiquated?" (p. 26), the passage in the Constitution referring to "attainder of treason" is Section 3 of Article III, not Article II.

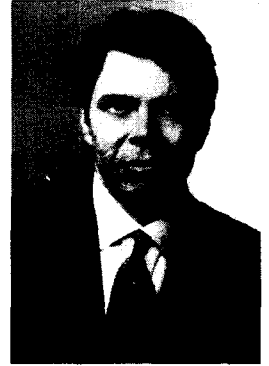
—SHELDON RICHMAN

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Thoughts on Freedom

by Donald J. Boudreaux



Two Indispensable Lessons

The 1900s are now history. I say “1900s” rather than “twentieth century” to avoid irritating those sticklers for precision who note that the final day of the twentieth century is December 31, 2000, and not December 31, 1999.

I agree, too, with sticklers of another sort who point out that, because time measurement is a human convention, there’s nothing special about January 1, 2000 (or about January 1, 2001). *Every* date—say, August 24, 1938, or June 7, 2097, or any other date you care to name—is the start of a unique 100-year period (and a unique 1,000-year period, and a unique 10,000-year period . . .).

Nevertheless, human conventions are real; they matter because people pay attention to them. While we shouldn’t impute mystical significance to our particular contrivance for marking time, it is indeed appropriate this month to reflect on the past 100 years.

What are the most critical lessons for us to learn from that century? I offer two candidates.

Shun Utopia

First, utopian schemes are disastrous. They should be avoided like the plague that they are. The trouble with any utopia—literally, “no place”—is that, by its very nature, its advocates do not tolerate deviations from their visions of perfection. They do not tolerate processes, growth, compromise, trial and

error, or that vital form of experimentation that Virginia Postrel calls “play.” This trouble is magnified a millionfold when the utopian scheme is enforced by the state, for then the arrogant task of defining and enforcing perfection is monopolized. There’s no longer the comfort of competing utopias—the ability to leave utopia A for utopia B (or, far more sensibly, to avoid utopia-ization altogether). When the state is in the utopia business, it alone defines *and insists upon* the standards that must be met. History proves the state’s ruthlessness at slaughtering anyone who might remotely not measure up.

Consider the twentieth century’s premier utopian scheme—communism. In exchange for unlimited state power, it promised everyone greater prosperity, security, equality, liberty, and cultural refinement. Instead, it delivered only destitution; its people were made “secure” only in the way that prisoners are secure; the masses were equally impoverished while their rulers enjoyed bounties of special privileges; liberty was crushed; and the resulting culture was hideous and grotesque.

Fascism and Nazism, of course, were utopian evils as well. They, too, justified unlimited state power as the means to earthly paradise. They, too, delivered destitution and terror.

What Thomas Sowell calls “the quest for cosmic justice”—the quest for utopia—inevitably leads to earthly hell.¹ If we learn only one lesson from the twentieth century, let it be that utopian visions are terrible, dreadful menaces.

Donald Boudreaux is president of FEE.

Keep Democracy in Perspective

The second lesson of the past 100 years is that democracy alone is insufficient for a society to be truly free and prosperous. Private property rights are far and away the most important bulwark protecting freedom and ensuring prosperity. Democracy, as such, guarantees neither. While this lesson is just as true as the one about utopia, it isn't as widely understood. After all, most of us alive in the West have been bombarded with paeans to democracy. Schoolchildren are taught that Western nations are free because they are democratic. Indeed, they are taught that freedom is synonymous with democracy. Voting = freedom = voting.

But voting does not equal freedom. Voting is merely the act of yanking a lever (or slipping paper into a box) every few years to register one among thousands or hundreds of thousands or millions or hundreds of millions of preferences for this or that candidate. The chance that any one vote will affect the outcome of any election is practically zero. No voter ever really chooses his or her representative—at least not in the way that each of us chooses an occupation, a house, a church, a college major, books to read, or a spouse.

In our everyday, nonpolitical lives—equipped as we all are with our private property rights—we routinely make choices that *count*. If you choose to buy a Ford rather than a Volkswagen, you get a Ford. What you get among the available options does not depend upon how others choose. You get what you want; everyone else gets what he and she wants. Not so in elections. You get only what a majority of the voting group wants. Thus, every time a decision is made collectively rather than individually, no individual is free. Each is a slave to the majority.

De-romanticizing democracy is frowned upon today, but I believe that it must be done. Democracy might be the most appropriate means of choosing government officials, but that does not imply that democracy equals freedom. Freedom requires more than the right to vote; it requires that each person be as unrestrained as possible from the arbitrary will of others—regardless of whether the others are conquering tyrants, hereditary oligarchs, black-robed judges, or a majority of neighbors or countrymen.

Private property is *the* indispensable protection from the arbitrary will of others, even when this arbitrary will results from a majoritarian election. Private property gives to each of us not only the assurance that others will employ themselves and their resources in ways that create prosperity for all, but also that each of us has a space that others cannot violate.

For evidence that private property rather than democracy is the key to prosperity and freedom, I point to India and Hong Kong. In India the electoral franchise is wide and elections have long been regular, but property rights are weak. For most of the post-World War II era, in contrast, Hong Kong had no democracy, but property rights there have been among the strongest the world has ever seen. Indians are poor and shackled by a massively corrupt state; the people of Hong Kong are wealthy and free.

Private property, not democracy, is the great guarantor of prosperity and liberty. And because it decentralizes power, it safeguards us from madmen with utopian hallucinations. □

1. Thomas Sowell, *The Quest for Cosmic Justice* (New York: Free Press, 1999).

The Government Is the Stabilizer?

It Just Ain't So!

Stability is the perennial issue in macroeconomics. The economist's judgment about the stability of the market economy stems from what Joseph Schumpeter called the "pre-analytic vision." To illustrate the point, Schumpeter specifically used John Maynard Keynes and his pre-analytic vision: Markets are inherently unstable; the government is the stabilizer. This belief, or vision, was held by Keynes years before he published his *General Theory* in 1936.

The most fundamental criticism of Keynesian economics has been offered by those who embrace the opposite vision: markets are inherently stable; the government is the destabilizer. This was the view of Ludwig von Mises and F. A. Hayek. The evidence of more than a half-century of failed "stabilization policy" strongly supports the Mises-Hayek view. The Keynesians can persist only by arguing that particular countercyclical measures were too weak or implemented too late. Underlying the whole debate, however, is a fundamental and enduring *conflict of visions*—to use the title concept of Thomas Sowell's 1987 book.

Writing for the *New York Times* (Week in Review, August 22, 1999), Louis Uchitelle asks, "Who You Gonna Call After the Next Bust?" His answer—and those of the authorities on whom he relies—are Keynesian in the most fundamental sense. Note the vision-bound assessment of Robert Pollin (University of Massachusetts): "[Markets] can't cure themselves. We will have to acknowledge that we need government for that. It's the stabilizer." And note that Princeton's Alan Blinder imputes the Keynesian vision to the public:

"In the event of a recession, people turn to Government *en masse*."

Though there is dispute at the most fundamental level, there can be agreement about the likely course of the economy in the months or years ahead. According to Uchitelle, "the eight-year expansion walks on precarious legs, and when it collapses, getting the American economy back on its feet could be surprisingly hard and painful." No doubt. But why, specifically, do we say the legs are precarious? And who, exactly, is supposed to be surprised that recovery will be hard and painful?

Uchitelle writes that "The strengths of this expansion are potentially destructive." (Read: Strengths are weaknesses; the market is inherently unstable.) He sees precariousness in the fact that "the current expansion is fueled by private-sector debt." Fueled? The Keynesian notion that the government can "fuel" the economy ("goose" the economy would be more apt) by deliberately spending more than it taxes has been uncritically transplanted to the private sector: "It is deficit spending that stimulates an economy, whether it comes from the private or public sectors." Particularly troublesome, according to Uchitelle, is the prospect that the private-sector stimulant will turn into a public-sector handicap when the bubble bursts. The government will then have to resort to deficit finance to stimulate an already debt-wracked private sector. It is as if the government "were starting a one-mile race from 100 yards behind the starting line."

Economists who understand the market's self-stabilizing properties find no special significance in private-sector debt. It doesn't fuel; it doesn't stimulate; it doesn't signify precariousness. Private-sector debt is simply the sum total of the indebtedness of many business firms and individual entrepreneurs. Most have borrowed on the basis of sound judgment and a healthy grasp of their particular economic circumstances. The profits they earn will put them in command of even more

resources in the months and years ahead. Some, though, have borrowed on the basis of faulty judgment. They will incur losses and will find themselves in command of fewer resources. This is the nature of the market process; this is the system of profit and loss.

Sign of a Problem

Exonerating private-sector debt per se does not mean that this debt is never a symptom of a problem. But what is the underlying problem? What accounts for the increased level of indebtedness noted by Uchitelle? Is it a credit expansion engineered by the central bank? Is it banking legislation that has encouraged financial institutions to take undue risks while the FDIC continues to provide deposit insurance at subsidized rates? Is it the too-big-to-fail doctrine that has guided regulators in dealing with overextended financial institutions?

It is, of course, all of the above. Centrally orchestrated credit expansion is the cause of boom and bust as spelled out by Mises and Hayek. Externalizing risks and subsidizing risk-taking behavior is another way of fostering an unsustainable boom. And the standard classical case for the system of profit and loss does not fully apply to a system of profit and too-big-to-fail. To recognize these aspects of our mixed economy is to understand that it is *because* of government policy that the private sector “walks on precarious legs.”

Though not noted by Uchitelle, a clear indicator of “precariousness” is the market’s perverse reaction to seemingly good economic news. Nowadays, when the unemployment rate goes down, speculators turn bearish. Why so? Isn’t lower unemployment a good thing? One view has it that the current unemployment rate (about 4.2 percent) is unsustainable, because it is significantly below the so-called natural rate of unemployment (generally believed to be 5 to 6 percent). The alternative view is that the natural rate itself has fallen.

In an unregulated market economy, the

question of which view is correct would be an idle one. But if a central bank is in charge of stabilizing the economy, the question takes on critical significance. Which view does the central bank think is correct? And what are the policy implications? With each movement of the unemployment rate, speculators reform their expectations about what the Fed is likely to do and when it is likely to do it. A central bank trying to manipulate the market while the market tries to anticipate and hedge against the central bank’s actions is not a recipe for macroeconomic stability.

So, who you gonna call after the next bust? If government is the destabilizer, it makes little sense to turn to that same government for stabilization. But the Keynesian economists are sure to make that very call, and the government is sure to respond. Recovery will be hard and painful. Who, though, will be surprised? Not the students of Mises and Hayek.

According to Pollin, acknowledging that we need government to provide stability “will open up a broader debate about what government should do.” Uchitelle has some ideas of his own here. The Federal Reserve, he argues, has had primary responsibility for stabilizing the economy over the past 20 years. It lowers interest rates when the economy begins to falter and encourages the private sector to take on more debt. Now, with private-sector debt at worrisome levels, we need to shift the emphasis from monetary policy to fiscal policy. Uchitelle sees room for old-line Keynesian programs: “More government spending on housing, public works, education and income subsidies seems likely to accompany the next recession.”

Students of Mises and Hayek would opt for decentralizing the monetary system rather than calling on the central fiscal authority to aid and abet the central monetary authority. But no. Suddenly, it’s 1936 again. Keynesianism is back—and in its rawest form. □

—ROGER W. GARRISON
Department of Economics
Auburn University

Across the Sea of Commerce

by Anthony Young

The Industrial Revolution, which brought about the age of steam, transformed ocean travel and shipping in the nineteenth century. It resulted in a paradigm shift in the size of ships and the speed with which they could cross the oceans. With this shift from sail to steam came a shift from wood to iron and steel. The skills, trades, and businesses needed to build these steamships grew dramatically as a result, providing employment for thousands of workers in Europe and North America in the nineteenth and most of the twentieth century. Ocean travel would only be eclipsed by the advent of flight.

The demand for travel and shipment of cargo spurred this technological shift, but there was another, often overlooked factor that drove the push to larger and faster ships: the mail. Everything from personal correspondence to important documents of all kinds could be delivered between Europe and the Americas only by oceangoing ships. Even in the mid-nineteenth century, the concept of “time-sensitive material” existed. Before the age of steam, the time to deliver mail between the European and North and South American continents literally depended on the wind. A typical crossing could take more than a month. A fixed timetable was impossible to establish.

In the late 1830s, the British Admiralty invited offers for monthly steamship service between Liverpool and North America for the

delivery of mail. Samuel Cunard won the contract by assuring the Admiralty and investors that the mail and passengers would cross the Atlantic on better steamships than theretofore built, depart on time, and arrive precisely as scheduled, all with strict adherence to safety. The British and North American Royal Mail Steam-Packet Company was founded on the motto “Speed, Comfort and Safety.” The first ship of this line was the *Britannia*; it made its first voyage to Halifax and Boston in 1840. Charles Dickens immortalized the spartan *Britannia* when he made the crossing in January 1842. His caustic observations of the trip were recorded in his slim volume *American Notes*. It would be decades before “luxury liner” would enter the vernacular.

No doubt it was the start of Cunard’s company that influenced the establishment of the White Star Line in Liverpool by John Pilkington and Henry Threlfall Wilson in 1845. Initially, White Star focused on the trade and passenger route to and from Australia. Additional competition came from America in 1850 when Edward Collins received a mail subsidy from the U.S. Congress. Collins planned to build four new steamships. The first was the *Atlantic*, followed by *Pacific* and *Arctic*. The latter two ships were the victims of maritime disasters. The fourth ship was never built, and Congress stopped funding Collins’s line in 1860.

There was competition from other nations as well. Between 1856 and 1862, three new steamship lines were founded: Germany’s

Anthony Young is a freelance writer based in Miami.

Hamburg-Amerika Line and North German Lloyd, and France's Compagnie General Transatlantique. The White Star Line was weakened by trying to compete in the fierce Atlantic passenger route and by internal corporate machinations. It attempted to merge with other steamship companies, but failed. The company never recovered, and its floating assets were liquidated. What remained, including the name, was purchased by 31-year-old Thomas Henry Ismay. His goal was to succeed in the transatlantic route where the old line had failed, using new, better appointed, and faster liners.

Ismay received the capitalization he needed from Gustav Schwabe in Liverpool. Schwabe agreed to finance the brash young entrepreneur on the stipulation that the new line would order its ships from the Belfast, Ireland, shipyard of Harland & Wolff. The reason? Schwabe's nephew was Gustav Wolff, a junior partner in Harland & Wolff.

This stipulation turned out to be a salvation for Harland & Wolff, which had been suffering from a decline in shipbuilding orders. With the creation of Ismay's Oceanic Steam Navigation Company in 1869, plans were immediately set to build five 420-foot steamers. Those ships were the *Oceanic*, *Atlantic*, *Baltic*, *Republic*, and *Adriatic*, all delivered between 1871 and 1872. Thereafter, Ismay's company kept the workers at the Harland & Wolff shipyards busy building cargo ships, passenger ships, livestock carriers, even several sailing ships—among the last built by the Belfast shipyard.

Aggressive competition among the British, German, and French shipbuilding and steamship companies had a tremendous ripple effect throughout the British Isles and Europe. Many companies were contracted to supply everything not built by the shipyards themselves, from the massive steam-driven engines to the marine chronometers placed on the ship's bridge to ensure precise time-keeping during the voyage. By itself, Harland & Wolff employed nearly 7,000 workers, performing such varied tasks as riveting the ship's hull plates to making intricate wood carving for the increasingly luxurious interiors.

A New Century Brings Larger Ships

By the turn of the century Germany had the fastest steamships plying the Atlantic. Hamburg-Amerika's *Deutschland* won the coveted Blue Ribbon in 1900 for its record speed between Europe and America. This award was then seized by North German Lloyd. The British could not catch the Germans, and this was a liability neither the White Star Line nor Cunard could easily surmount at first. The French merely sniffed. But it was Cunard that figuratively fired the shot across the bow of its competitors when it launched the *Mauritania* and *Lusitania* in 1907. These two ships truly were superliners with regard to their size, speed, and appointments.

The *Mauritania* and *Lusitania* were over 780 feet long and weighed in at over 31,000 tons. They each carried 560 first-class passengers, 475 second-class passengers, and 1,300 third-class, or steerage, passengers. But the marvel of these ships lay deep within. Powering these two liners were steam turbines, not steam reciprocating engines. The *Mauritania* set a new transatlantic record of 23.69 knots, recapturing the coveted Blue Ribbon. Cunard now had two powerful weapons in the battle to gain supremacy of the North Atlantic.

Cunard embraced steam turbine technology out of necessity, but it was a fearsome gamble. This new technology was pioneered by Charles Parsons, who founded the Steam Turbine Company in 1894. While the steam turbine was nothing new, in a marine application it was uncharted territory. Within three years Parsons had developed the world's first steam turbine in a small cutter named *Turbinia*. Sea trials were completed in 1897. In a brash display of showmanship before a flotilla of ships celebrating Queen Victoria's Diamond Jubilee, the speedy cutter left all witnesses agog. Also witnessing the display of speed were Thomas Ismay and his son Bruce. Parsons drew up to the Ismay's ship and invited the two men on board to go for a spin. The Ismay's were astounded at the top speed of 40 miles per hour. Later, they discussed the possibility of building steam turbines for future passenger liners with Parsons, but it was

Cunard that took the plunge in using the new engines in the *Mauritania* and *Lusitania*. It was a gamble that paid off for Cunard.

With these two ships, the gauntlet had been thrown down before the White Star Line. J. Bruce Ismay had taken over direction of the Oceanic Steamship Navigation Company and the White Star Line on the death of his father. However, the company was no longer independent. In 1902, Ismay's company had been purchased by J. Pierpont Morgan and added to his formidable International Mercantile Marine Company. Many in British financial circles worried over the ownership of the prestigious White Star Line by an American company and what it might do. In fact, it turned out that the infusion of capital by Morgan's company would permit the White Star Line to take on the *Mauritania* and *Lusitania*.

The *Titanic*

Not long after the launch of Cunard's two new superliners, Ismay was invited to the palatial home of Lord Pirrie in London. Pirrie had risen through the ranks at Harland & Wolff to become managing director. He wielded tremendous power and was admired and respected on both sides of the Atlantic. He saw Cunard's two new ships as a threat to the White Star Line. With a virtual lock on all ships built for the Ismay's company, Pirrie invited Ismay to dinner to discuss a proposal for two luxury liners to surpass Cunard's ships. Ismay stated Cunard's new ships would affect the White Star Line's bottom line unless something dramatic was done. Pirrie outlined the size, capacity, and gross tonnage of the liners he believed the White Star Line should have, and Ismay was in complete agreement. Ismay assured Pirrie he could secure financing from J.P. Morgan. They agreed to proceed immediately with plans for two new super ships. While Pirrie went back to discuss the possibility of building the ships with his key "splendid men," as he called them, Ismay sailed for New York to put the proposal before Morgan.

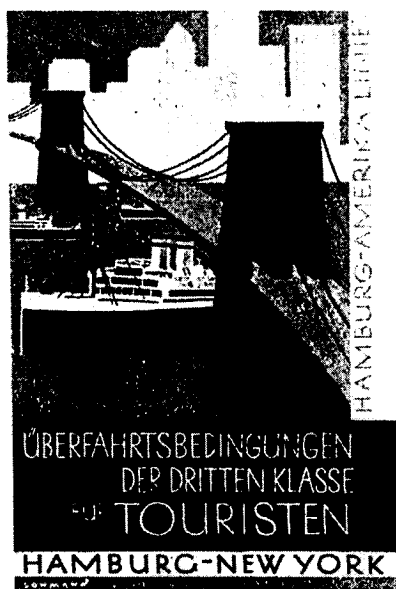
It came as no surprise to Ismay that Morgan backed the idea. Morgan wanted the White Star Line to eclipse Cunard, and the two ships certainly sounded as though they could do it.

Ismay related the details to Pirrie. Out of those and subsequent meetings evolved the design of the *Olympic* and *Titanic*. The ships would be 882 feet long, have a 92-foot beam, and weigh more than 45,000 gross tons. They would each carry 410 first-class passengers, 300 second-class, passengers, 1,000 third-class passengers, and a crew of nearly 900.

The three large construction slips at Harland & Wolff's shipyards were torn down and in their place rose two massive slips to begin work first on the *Olympic* and later the *Titanic*. The keel of the *Olympic* was laid on December 16, 1908, that of the *Titanic* on March 3, 1909. The *Olympic* completed her fitting out and ocean trials by the spring of 1911 and took her maiden voyage in June. The Royal Mail Steamship *Olympic* was the largest ship in the world and was everything the White Star Line had promised. Cunard now had a new nemesis, and another was on the way. The following year, the *Titanic* was launched, with its maiden voyage set for April 1912.

Work began on a third liner, called the *Gigantic*. The name was later changed to *Britannic*, a decision that may have been influenced by the sinking of the *Titanic* after it struck an iceberg on the night of April 14, 1912. The tragic event, with a loss of over 1,500 passengers and crew members, has proved to be a never-ending story. Captain Edward J. Smith and Thomas Andrews of Harland & Wolff were among the casualties. However, J. Bruce Ismay survived. He stepped down as chairman of the White Star Line the following year. The decision to step into a lifeboat would haunt him for the rest of his life.

The *Olympic* returned to Harland & Wolff for extensive modifications to its hull, additional lifeboats, and other changes, which were incorporated into the new *Britannic*. Cunard and the German and French lines reviewed and modified their ships in light of the disaster. Besides the loss of the *Titanic*, the human toll, and the damage to its reputation, the White Star Line faced new competition from Germany, which was building its own superliners. The first was the *Imperator*, launched in 1912, which could carry 5,100 passengers and crew members. The *Vaterland* entered service in 1914. The third and largest



ship, the *Bismarck*, was due to go into service later that year. These new ships of Holland-America were a threat to Cunard and the White Star Line, with interiors and accommodations that rivaled the British lines.

The peaceful battle for the Atlantic ended with the outbreak of World War I in August 1914. In 1915 the British Admiralty requisitioned the liners of Cunard and the White Star Line and other commercial ships for use as hospital and troop transport vessels. Prowling German U-boats immediately halted passenger crossings. In May 1915 the *Lusitania* was struck by a German torpedo and sank in only 20 minutes. In November 1916, the *Britannic* struck a mine and sank in 55 minutes, despite its double hull.

The ships of Germany fell to a different fate. The *Vaterland* was seized by the United States while at port in New York. She was converted to a hospital ship, christened *Leviathan* and entered service in 1917. *Imperator* was also seized by the United States but saw no wartime service. After the war, the United States kept the *Leviathan* and Cunard received the *Imperator*. The Treaty of Versailles stipulated that the *Bismarck* would be finished and handed over to the British as part of the war reparations. The White Star Line acquired the ship in 1922, and renamed it the *Majestic*.

The French line got through the war

unscathed. Its original ship, the *France*, had its maiden voyage in 1912. It was joined after the war by the *Paris*, later by the *Ile de France*, and in 1932 by the sumptuous *Normandie*. What was left of the two German lines merged and eventually launched the *Columbus*, *Bremen*, and *Europa*. A new Italian line emerged during the '30s with the *Rex* and *Conte de Savoia*. No new British liners entered service until the *Queen Mary* in 1935 following the merger of Cunard and the White Star Line. The *Queen Elizabeth*, at 80,000 tons, launched in 1940. The Depression had a significant impact on transatlantic travel but the numbers began to climb again in the late '30s.

World War II brought transatlantic ocean travel to a virtual halt once again, and these mighty liners reprised their roles as hospital ships and troop transports. Together, the *Queen Mary* and *Queen Elizabeth* moved over one million troops. After the war only the British and the French lines continued to cross the Atlantic with passengers.

The Jet Age

Transatlantic flights became a realistic possibility in the late 1940s. TWA was the first airline to fly the sleek Lockheed Constellation from Washington to Paris at 300 miles per hour in February 1946, making the trip in 12 hours. In 1948 the airline started luxury all-sleeper service, and later instituted "Sky Tourist" class for low-cost travel between the United States and Europe. However, many travelers relished the leisure, quiet, and luxury the ships provided. In fact, 1957 marked a postwar peak with more than one million passengers opting for the opulent liners. When the first American commercial jet flew to Paris in only seven hours on October 26, 1958, the intercontinental jet age was born. By 1960, 70 percent of the travelers between America and Europe were flying in jets.

The superliners had entered a twilight era. The only liners operating by the '70s were the *QE2* and the new *France*. The *United States* had entered service in 1952 and was retired in 1969. Today, only the *QE2* travels the Atlantic. Those who take her do so because for them, it is the only way to cross. □

How to Sink a Car Ferry

by Andrew P. Morriss

I recently had the opportunity to travel on a rare form of transportation—one that receives no government subsidies. The *S.S. Badger*, a ferry operated by the Lake Michigan Carferry Service, makes twice daily trips between Ludington, Michigan, and Manitowoc, Wisconsin, from mid-May to mid-October, carrying up to 180 automobiles and 620 passengers. For only \$81, I was able to avoid driving through Chicago and spent the four-hour trip relaxing on a lounge chair on deck. I also had the chance to enjoy a movie, eat, shop, or visit a museum on board. State-rooms are available.

Ships began regularly carrying freight across Lake Michigan in 1875. The first car ferry, the *Ann Arbor* No. 1, began service in November 1892 between Kewaunee, Wisconsin, and Frankfort, Michigan, ferrying railroad cars across the lake to eliminate transferring cargo between trains and boats at each end. By the 1950s car ferries had expanded to carry automobiles and passengers as well as train cars. In 1955, the peak year for the ferries, the Chesapeake & Ohio (C&O) Railway's seven car ferries carried 205,000 passengers, 71,000 automobiles, and 204,460 freight cars on 6,986 crossings among multiple Lake Michigan ports.

During that same time, the Ann Arbor Railroad was also operating five car ferries

between Frankfort, Michigan, and four other lake ports. Although thousands of people crossed the lake on the not-particularly-comfortable ships, the railroads kept their emphasis on year-round boxcar transport, and passenger amenities like scheduled departures and food service were few. Rail-traffic demand for ferry service was declining, however. By the 1960s diesel train engines could pull 150 rail cars at 50 miles an hour around the rail bypass of Chicago with a crew of five or six, while a ferry, with its crew of 50, could carry only 20 freight cars at a time.

Railroads were heavily regulated by the federal government, so they could not simply stop uneconomical services. With the railroads losing millions of dollars a year on the ferries, the 1970s saw repeated attempts to secure Interstate Commerce Commission's (ICC) permission to abandon service.

The Chessie System (the C&O's successor) finally got out of the ferry business by turning over its three remaining ferries to a company formed by a Ludington businessman, the Michigan-Wisconsin Transportation Co. (MWT), in 1983. In a measure of how desperate the railroad was to shed its regulatory burden, it gave the MWT its last three ferries, which had a tremendous scrap value, for three dollars plus the MWT's agreement to assume the Chessie's federally mandated obligation to pay the ferry workers for six years even if the boats did not sail at all.

The MWT continued to operate the car-ferry service year-round as a combined

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freight and passenger operation, as it was required to do as a railroad under ICC rules. Even so, 80 percent of its revenue came from the summer tourist trade and only 20 percent from the year-round freight business. The failure to get out of the railroad business doomed the MWT. It ceased operation in November 1990 and filed for bankruptcy.

New Beginnings

When he learned that the MWT was planning to cease operations, local entrepreneur Charles Conrad stepped in to save the ferry. Conrad's father, James, had spent 35 years working for Pere Marquette Railway, mostly as chief ferry engineer. "I spent a lot of my time with him crossing the lake," Conrad told an interviewer in 1992. "Those ferries were a big part of my childhood."

After a few years working on the ferries Conrad went on to a successful career as an entrepreneur. In 1962 he started Thermotron Industries, a maker of test chambers for everything from electronic circuitry to airplanes, with \$1,000 and just one employee (himself). When he retired 18 years later, it had 550 employees and \$18 million in annual sales. Conrad sold the company for an estimated \$7.5 million.

Finding retirement not exciting enough, Conrad formed a company to restart the ferry service as a passenger and automobile service. He negotiated a deal with the MWT to buy the three ferries. A few months before the scheduled launch of the new service the MWT declared bankruptcy, however, and the bankruptcy court blocked the deal, ruling that open bids were required. Despite the possibility he would not get to buy the ships, Conrad invested another \$1 million in renovating the *S.S. Badger* to ensure that he would not miss the scheduled launch date if he got the ships. Ultimately Conrad prevailed in the auction, paying \$500,000 for the ferries and investing \$1.5 million on improvements to launch the service with the *Badger*.

For the first year of service, Conrad hoped for 80,000 passengers—he got 115,000 and extended the sailing season to October 11 to meet the increased demand. The new service

turned a profit its first year, and the surrounding area boomed. More recent estimates put the ferry's economic impact at over \$20 million each in Michigan and Wisconsin.

The Role of the Entrepreneur

The key to Conrad's success was the transformation of the car ferry service from an extension of the railroad into a tourist oriented mini-cruise line. "This is really a whole new industry because now we are ferrying people instead of rail cars," Conrad said in 1992. Although passenger traffic started in the 1940s, the railroads never marketed it to the public.

The focus on passengers brought a new emphasis on service as well. "We're going to emulate Disneyland and Disney World as much as possible," Conrad said. "We're going to give customers the highest quality of professional services they'll find anywhere." A stickler for detail, he insisted on on-time departures and keeping the brochure racks full in the ticket office—a marked change from the railroad's practice of refusing to run on a fixed schedule. He brought in experts to train his employees to ensure that everyone who got on board had a good experience. The crew was expanded to provide on-board entertainment—50 of the 60 crew members now concentrate on passenger services from the free "Badger Bingo" to puppet shows for children.

Much of the publicity surrounding the ferry's new start under Conrad focused on his love for the Ludington area as a motive for his actions. "He didn't buy the ferry to make money, and I think everyone ought to know that, if they don't already," Bruce Beda, a Milwaukee businessman and friend of Conrad's, told an interviewer. "He's running this ferry because he cares about helping his community."

It's possible the 74-year-old Conrad didn't care about increasing his personal fortune through his investment in the car ferry, although I doubt he intended to throw his money away. It is impossible, however, that he didn't care about making money. Unless the ferry made money it wouldn't last.

Entrepreneurs succeed by filling a need others haven't noticed. The railroads didn't notice that their freight ferries had become passenger ferries, and they failed to adapt. The railroad union didn't notice that unprofitable operations meant eventual closure. But Charles Conrad saw what others did not and created a profitable enterprise in a single year where others had lost millions for decades. His idea produced a legacy of a profitable car ferry, something that will continue to benefit the economies of Ludington and Manitowoc, and tourists like me, for years to come.

Conrad sold the ferry business to some of its executives in fall 1994 and died in February 1995.

His entrepreneurial skills and interest were obviously critical to the revival of the car ferry. But just as important was the federal government's and the state of Michigan's willingness to get out of the way of the transformation of the railroad car ferry into a passenger-oriented seasonal service. The ICC allowed the service to be classified as a passenger ship instead of a railroad, eliminating the requirement that it run 12 months a year and carry freight trains. The state exempted coal-burning ferries from some air pollution requirements. The company also took advantage of a new state law to negotiate an agreement with the state so that the new company would not be responsible for its predecessors' contamination of the dock site, an agreement critical to getting the service started.

Note the important difference between what Conrad and what the government brought to the project. Conrad supplied the capital, the know-how, and the idea. The government kept its hands off. It didn't require uneconomic service. It didn't burden the 1940s-built ship with 1990s air pollution regulations. It didn't require the company to pay for the environmental sins of unrelated prior owners of the site. It didn't subject the company to the burdensome regulations that governed railroads. Any of those things could have killed the project. What the state brought to the table was a willingness to refrain from destroying the project before it could start. Sadly, we live in a society where that happens all too infrequently.

Stormy Waters Ahead

Unfortunately, the hands-off approach may be changing. Inspired by the new company's success, other Lake Michigan towns are looking to revive their car ferries. Instead of seeking entrepreneurs, however, they are turning to the federal and state governments for subsidies. Looking north to the Ludington-Manitowoc ferry, Milwaukee officials determined they should have a ferry too. Although they discussed service with the Lake Michigan Carferry twice, negotiations ultimately failed. The two sides differ sharply over the reasons for the failure. The Carferry charges that the city demanded hundreds of thousands of dollars in "landing fees" and refused to participate in marketing efforts. The city claims the Carferry demanded operating subsidies as the price of starting service and couldn't deliver the type of service needed by the Milwaukee market.

Despite their failure to interest the only successful ferry operator in the area, Milwaukee officials pressed ahead. "It is kind of logical we should have it," Milwaukee Mayor John Norquist said during a 1994 budget hearing on a request for \$500,000 in city funds to study the idea.

Getting Milwaukee the ferry service politicians think it should have apparently takes quite a bit of government help: for starters, \$80 million in loan guarantees from the U.S. Maritime Administration to build high-speed hovercraft and a \$650,000 loan from the state of Michigan to the town of Muskegon for a dock. The loan guarantees are essentially a way for private entities to borrow on the government's credit rating rather than their own; the guarantees can shave several percentage points off interest costs and allow longer-term financing than would otherwise be available from private investors. Of course, if the borrower goes bust, the taxpayers are left paying off the loan.

Local newspapers also quickly uncovered disturbing facts about Hydrolink, the company chosen by state officials to launch the new ferry service. Its only known investor, a Wisconsin neurosurgeon, has a less than confidence-inspiring past: two bankruptcy filings since 1990, and guilty pleas to nine counts

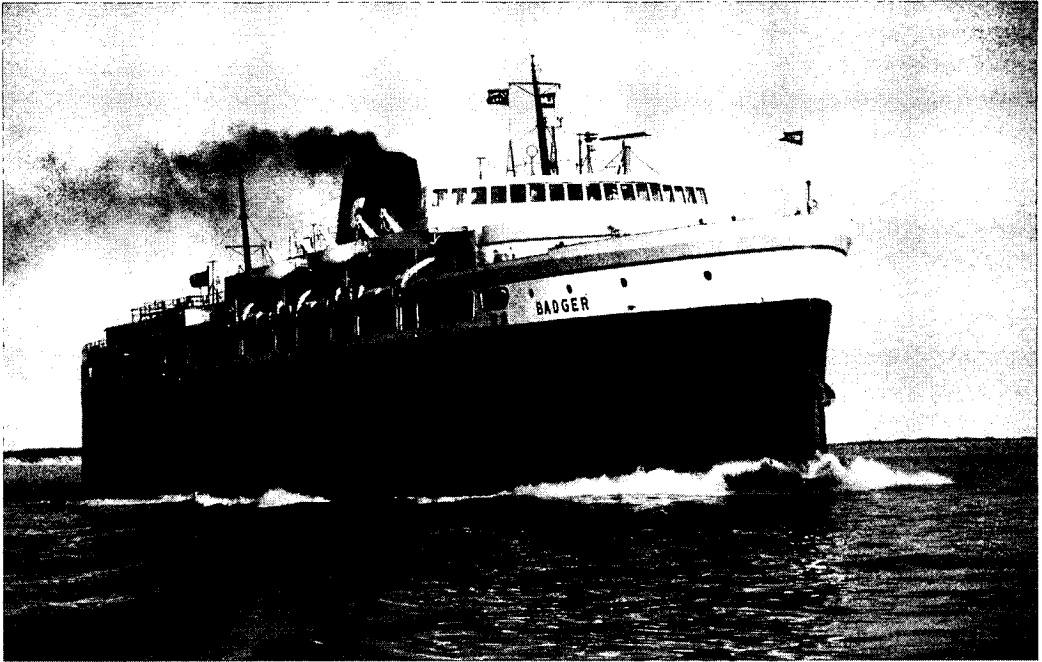


PHOTO BY ANDY KLEVORN

Lake Michigan Carferry—S.S. Badger

each of false swearing, forgery, and filing fraudulent sales tax returns, and quite a few malpractice charges lodged against him with state regulators. (In a boost to public confidence, the company won't disclose the identities of any of the other investors.)

The new ferry may yet run aground. One sign of trouble for a politically structured proposal is when politicians start distancing themselves from the opportunity to hand out tax dollars instead of lining up to do so. U.S. Representative Peter Hoekstra, whose district includes both Ludington and the proposed new ferry's docking site, Muskegon, was one of the first to jump ship. Although he initially told the *Grand Rapids Press* that "it's pretty typical" that congressmen are asked if they agree with loan guarantees for constituents, four days later he told Ludington officials that "I am not sure how much influence a congressman can have on an issue like this."

State officials aren't rushing to claim credit for their contributions either. Michigan Governor John Engler's spokesman said the administration was merely approving projects based on voter-approved criteria. "We just determined: Does the project have economic

development potential? And is it good for the environment and does it clean up the waterfront? We had to pick the best projects based on how they were written." The state concedes it didn't consider whether the project would compete with an existing business.

Michigan and Milwaukee officials have been engaged in a great deal of doubletalk to conceal the subsidies. The subsidized docks aren't a subsidy because anyone could use them. The loan guarantees aren't a subsidy because no money changes hands (until a default!). Ludington residents, however, have no doubts about what the state support and federal loan guarantees mean: "We're not opposing high speed ferry service," said William Kratz, executive director of the Mason County Economic Development Alliance. "What we're opposing is the taxpayer subsidy of one private business versus an existing, nonsubsidized private business." The existing ferry company also sees through the Engler administration's obfuscation: "We do consider the grant to be a financial subsidy that gives potential competition a significant advantage." All agree—subsidizing a competitor would be a good way to

sink the private-sector success story, leaving the taxpayers holding the bag on Hydrolink's loans.

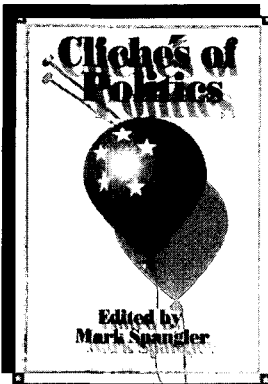
The unfairness of subsidizing a competitor to an existing private business is sometimes obvious even to politicians. The logical answer is not to subsidize either. Not surprisingly, some local politicians had a different response. One Michigan state senator said that "If the state has made its decision to be in the subsidy business on this, there's going to have to be parity for Ludington."

Subsidizing both services isn't even a second-best alternative. Not only could government subsidies lead to the same kind of regulatory nightmare that sank the railroads and their car ferries, but forcing unasked-for subsidies on the private firm wouldn't level the playing field. The Lake Michigan Carferry Service is turning a profit without a subsidy. Hydrolink can't even float a boat without subsidized loans. Even if equal dollar amounts of subsidies went to both, the value of the subsidies to Hydrolink would be much greater. The real choice should not be between one subsidy or two (or three or four . . .) It should be between one subsidy or none.

The Superiority of Private Enterprise

Even a quick look at the contrast between the Ludington ferry and the proposed Milwaukee ferry shows the superiority of the unsubsidized service. One ferry was started as a labor of love by a successful entrepreneur who invested more than \$2 million dollars of his own money. The other is backed by city officials who stand to enhance their own standing and a convicted forger, subsidized by massive government loan guarantees and direct expenditures. One is the result of years of involvement in the local community and resulting insights into the local economy. The other is the result of a politician's desire to get what is "kind of logical" implemented despite the lack of a private sector response. The difference between the market's and government's responses couldn't be clearer.

The ferries were almost sunk for good once by government regulation of the railroads. Let's hope that Michigan and federal officials come to their senses and remember how they helped save the Ludington ferry—by doing nothing. □



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A Tribute to the Jitney

No person shall operate or cause to be operated any jitney upon any street, avenue, boulevard or other public place within the City of Detroit whether such jitney operates wholly within the City of Detroit, or from some point within the City of Detroit or to some point outside of the City of Detroit to some point within the City of Detroit.

So reads the official ban on one of the oldest illegal businesses that still operate openly in Detroit, Michigan. The rather emphatic language says, in effect, “We don’t want any part of this!” And yet on public bulletin boards at grocery, drug, and department stores all over the city, one can find notices that announce, “For Jitney Service, Call This Number.”

Just what is this “jitney” thing that the City of Detroit, in the name of protecting the public, officially declares *verboden*? It’s a very popular business in which mostly retired autoworkers, church deacons, widowers, and otherwise idle but able citizens charge a small fee to give poor people a ride from where they shop to where they live.

The crime is that jitneys do their good work without a taxi license from the city government—the same city government that wouldn’t authorize a single additional taxicab for 50 years. Getting a license to do just about anything in Detroit means endless delays, lengthy

waiting lists, mounds of paperwork, and senseless rigmarole.

Thriving Business

Fortunately, the cops in Detroit look the other way and the jitney business is thriving. According to the *Detroit Free Press*, no one has filed a complaint against a jitney in at least 26 years and no jitney driver in recent memory has had to face the stipulated fine of \$500 and 90 days in jail. Nearly a third of Detroit’s households don’t have cars, and the city has one of the lowest per capita incomes of any urban area in the nation, so it’s likely that thousands of technically illegal jitney rides occur there every week. The drivers charge much less than the taxicabs (which many of their customers cannot afford), often carry their clients’ bags from the store to the vehicle, are easily accessible in any neighborhood, and are the primary means of transportation for Detroit’s poor.

The spontaneous order that Detroit’s jitney system has produced is elaborate as well as efficient. According to a report from the Washington, D.C.-based Institute for Justice:

Although the jitney drivers in Detroit do not at first seem to be organized, the structure of jitney service is actually quite complex. While there is little camaraderie and no formal organization of jitney drivers, the market produces a structure of needs and services. . . . [They] operate mostly out of strip mall shopping centers. . . . Most jit-

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ney drivers will not service the whole shopping center but will attach themselves to one store. Thus, each driver has his territory. Well-known jitney drivers often will transport the store's employees to and from work as well.

Assurance of driver reliability is handled nicely by the market itself. Word of mouth directs store employees and customers to particular drivers, who tend to live in the areas they serve. Owners of stores vouch for certain drivers by issuing them cards that are placed prominently in windshields. Drivers seem to prefer this private certification of competence to licensing. "When asked about the possibility of jitney licenses," says the Institute for Justice, "many drivers are suspicious of what it would mean to have to deal with the bureaucracy at the City/County Building."

Jitneys aren't special to Detroit. They operate in most major American cities in direct but illegal competition with both the government-sanctioned taxi monopolies and government-run bus systems. In some places, they face a lot more harassment from the authorities than they do in Detroit.

In New York City, the police bust jitney drivers all the time. Writing in the *New York Times Magazine* of August 10, 1997, John Tierney tells the story of an immigrant from Barbados who spent years trying to go the legal route and get a license to transport residents around the city in his van. His application included more than 900 supporting statements from riders, business groups, and church leaders. He was approved by the City Taxi and Limousine Commission and supported by Mayor Rudy Giuliani. But in the end, the city council did what it has done with almost every such request: it rejected his application. Now this outlaw entrepreneur and thousands just like him in the Big Apple dodge the cops every day as they earn a living and their customers' approval.

Jitneys have a long and honorable tradition in America. According to two California eco-

nomic historians writing in the October 1972 *Journal of Law and Economics*, the first one appeared in 1914 in Los Angeles, when L. P. Draper accepted a fare from a stranger in exchange for a brief ride in Draper's Ford Model T. The fare was a "jitney"—slang for a nickel—and it became the industry's standard fee for many years thereafter. By the autumn of 1915, a thriving jitney industry was providing inexpensive and reliable transportation in cities from San Francisco to Portland, Maine.

It didn't take long, however, for public officials and their friends in the electric streetcar industry to start piling on regulations with the aim of running the jitney competition out of business. *The Electric Railway Journal* called the jitneys "a menace," "a malignant growth," and "this Frankenstein of transportation."

During World War I, the American Electric Railway Association even suggested that jitney drivers be drafted into the military. It called for the War Industries Board to "suppress entirely all useless competition with existing electric railways" and argued that "men engaged in nonessential automobile service of this nature should be forced to obtain some useful occupations or compelled to enter the service."

Electric railways aren't around much anymore, but taxicab and city bus monopolies have taken their place in the war against jitneys. Laws against jitneys and the victimless crime of helping people get around town without a license, whether fully enforced or not, represent a cynical use of the police power of government by special interests. They are evidence of corrupt and stupid politicians who often express sympathy for the poor at the same time they make war on poor entrepreneurs.

The persistence of jitneys on America's streets is an inspiration, a testimony to the power of the profit motive that fires up people to help people even when it's illegal to do so. As to the war against them, Mr. Bumble's famous line from Dickens's *Oliver Twist* comes to mind: "The law is a ass." □

The Law of Supply and Demand

by Israel M. Kirzner

The theory of supply and demand is recognized almost universally as the first step toward understanding how market prices are determined and the way in which these prices help shape production and consumption decisions—the decisions that make up not only the skeleton, but also the flesh and blood of the economic system. Austrian economics thoroughly agrees with this. However, when we dig just a little below the surface of the “law” of supply and demand, we encounter difficulties that have, directly or indirectly, led Austrians to explain the determination of prices differently from how it is often, at least implicitly, presented. I will try to explain the sense in which Austrians are unhappy with the textbook presentations of supply and demand—and are yet fully in agreement with the *general* emphasis on supply and demand as being the key to economic understanding.

The Basic Proposition

The basic insight underlying the law of supply and demand is that at any given moment a price that is “too high” will leave disappointed would-be sellers with unsold goods, while a price that is “too low” will leave disappointed would-be buyers without the goods they wish to buy. There exists a “right” price, at

which all those who wish to buy can find sellers willing to sell and all those who wish to sell can find buyers willing to buy. This “right” price is therefore often called the “market-clearing price.”

Supply-and-demand theory revolves around the proposition that a free, competitive market does in fact successfully generate a powerful tendency toward the market-clearing price. This proposition is often seen as the most important implication of (and premise for) Adam Smith’s famed invisible hand. Without any conscious managing control, a market spontaneously generates a tendency toward the dovetailing of independently made decisions of buyers and sellers to ensure that each of their decisions fits with the decisions made by the other market participants. Were this tendency to be carried to the limit, no buyer (seller) would be misled so as to waste time attempting to buy (sell) at a price below (above) the market-clearing price. No buyer (seller) would in fact pay (receive) a price higher (lower) than necessary to elicit the agreement of his trading partner. To the extent that this proposition is valid, free competitive markets achieve what F. A. Hayek has justifiably called a “marvel.” But it is in regard to the validity of this proposition (and in particular to our reasons for being convinced that this proposition is both valid and relevant) that Austrians differ sharply with mainstream textbook economics. And it is precisely because of the universally acknowledged centrality of the supply-and-demand proposition

Israel Kirzner is a professor of economics at New York University and author of The Meaning of Market Process. This is the first in a series of articles laying out some foundational elements of modern Austrian economics.

for all of economics that this disagreement is so important.

The Role of Knowledge

The mainstream textbook approach to this proposition is, in one way or another, explicitly or implicitly, based on the assumption of perfect knowledge. The Austrian approach does not make the perfect-knowledge assumption the foundation for this proposition; quite the contrary, Austrians base the proposition squarely on the insight that its validity proceeds from market processes set in motion by the inevitable *imperfections* in knowledge, which characterize human interaction in society.

In certain respects the mainstream view is not unreasonable. In many contexts we generally take it for granted that human beings are aware of the opportunities available to them. When economists believe, for example, that a price increase will cut the quantity people seek to purchase, and a price decrease will stimulate sales, this belief is based on the reasonable assumption that such price increases or decreases are in fact likely to become known to prospective buyers soon enough to make a difference.

The mainstream view takes this not unreasonable assumption and pursues it relentlessly, in effect, to its logical—but no longer quite so reasonable—conclusion. This conclusion is that in any free market, the market-clearing price is *instantaneously* (or, at least, *very rapidly*) established. If every market participant knows what every other market participant is prepared to do (including, especially, the quantity he is prepared to buy or sell at any given price), it follows that any price higher than the market-clearing price cannot emerge (since prospective sellers would realize that they would be left with unsold goods). It follows, similarly, that any price lower than the market-clearing price cannot emerge (since prospective buyers would realize that they will be left without the goods they wish to buy and for which they are in fact prepared to pay a higher price if necessary). The proposition that free-market prices are thus inevitably market-clearing prices proceeds

inexorably from the belief that market prices are, in effect, instantaneously known to all potential market participants.

The Dangerous Assumption

The assumption that all market participants are always fully aware of market opportunities in which they might be interested is often presented, in mainstream textbook expositions, as part of the assumption of so-called “perfect competition.” Perfect competition *explicitly* presumes universal market omniscience. One way of expressing the Austrian unhappiness with the mainstream textbook treatment is to point out that to start supply-and-demand analysis by assuming that competition is “perfect” (in the textbook sense) is not only to be wildly (and therefore unhelpfully) unrealistic; it is in fact also to rob the analysis of all significant economic content—since the principal results sought to be shown turn out to be simply statements repeating the governing assumption in slightly different language.

To demonstrate that the interplay of supply and demand in a free market generates a powerful tendency toward the market-clearing price is to meet a daunting analytical challenge. To demonstrate that in a perfectly competitive market the only possible price is the market-clearing price is simply trivially to identify what has already been planted in the initial assumption. To unpack the mathematically implied properties of a definition *may*, of course, be a significant (mathematical) contribution. But to demonstrate the attainment in free markets of the market-clearing price by restricting analytical attention to the situation in which this price is the only one permitted to be conceivable, is, as a matter of *economic* analysis, a hollow triumph indeed.

This difficulty that Austrians find with the textbook discussions of supply and demand can be presented in somewhat different terms. The traditional classroom blackboard demonstration of the law proceeds by drawing the classic supply-and-demand diagram—a downward sloping demand curve intersecting an upward sloping supply curve. (For present purposes we forgo the details surrounding the construction of this diagram; it is one familiar

to the hosts of students who have ever been exposed to elementary economics.) The core of the classroom analysis generally consists of discussion showing, first, that any market price higher than that indicated by the intersection of the two curves (that is, a price higher than the market-clearing price) must tend to produce competitive pressure toward a decrease in price (since the high price will generate a surplus of unsold merchandise); and second, that any market price lower than that indicated by the point of intersection must produce competitive pressure toward an increase in price (since the low price will generate a shortage of goods offered for sale, as compared with the quantities prospective buyers wish to buy).

Austrians do not have serious disagreement with such discussions in themselves; they simply point out that those discussions are utterly inconsistent with the assumption of perfect competition (which textbook analysis takes as its operative assumption). A little careful analysis of the perfect-competition assumption (which analysis can, however, unfortunately *not* be fitted into this space) suffices to show that under perfect competition *there cannot in fact exist two curves* (the demand curve intersecting with the supply curve). Under perfect competition the supply-and-demand diagram

shrivels instantly *to a single point*—the point where the two curves *would* have intersected (*had* the curves themselves existed!). This is so because any point on a market supply curve or on a market demand curve that is *not* that intersection point can have analytical existence only by suspending some or all of the conditions that define the state of perfect competition. The diagram (valuable though it certainly is!) is simply not consistent with the assumed conditions under which it is supposed to be operating.

Our discussion has unfortunately been overwhelmingly negative. We have pointed out problems that Austrians have with mainstream supply-and-demand analysis—but we have not suggested how an alternative approach might avoid these difficulties. Subsequent articles in the present series will attempt to fill this gap. For Austrians, the law of supply and demand, properly explained, is at least as centrally important for economic understanding as it is for mainstream economics. We will show how Austrians deploy insight into the *entrepreneurial* character of dynamically competitive markets (insights that can have no place within the mainstream textbook paradigm) to explain the law of supply and demand in an intuitively and analytically satisfying way. □

Next Month's *Ideas on Liberty*:

Our February issue features
 "The Day We Read No More,"
 "Lessons from the Chicago Fire,"
 "A Camera Reaches 100,"
 and much, much more.

Plus: Professor Kirzner continues his series.

Don't miss it!

Why Crime Declines

by Bruce L. Benson

Crime in America has fallen since 1991. In that year, the reported crime rate compiled in the FBI's Uniform Crime Reporting program peaked at 5,897.8 per 100,000 population. Then it dropped almost continuously, reaching 4,922.7 in 1997. Preliminary statistics for 1998 indicate a 7 percent drop below the '97 figure. (Monthly statistics suggest that the trend continued in 1999.)

Why? Politicians have ready answers. They claim credit through their support of prison construction, longer mandated sentences, greater police funding, and so on. They also claim credit for the strong economy and low levels of unemployment, which reduce the incentives to commit property crimes. Police point to their efforts in the war on drugs or to innovations in policing strategies such as "community policing." Criminologists cite many of these same causes, along with the changing age distribution of the population: the number of crime-prone young males has been shrinking thanks to aging and reduced birth rates.

No doubt many and probably all of these things work together to help explain falling crime rates, but there is another, perhaps even more important factor that has gone largely unnoticed. Private citizens have responded to

the fear of crime by investing increasing amounts of their own time and money in crime prevention.

Private-sector responses to crime have taken many forms, including crime watch and other types of neighborhood or building watching, patrolling and escort arrangements, installation of alarms and other detection devices, improved locks and lighting, investments in self-protection such as martial-arts training and guns, and employment of private security personnel. All these activities have been increasing dramatically as crime rates have fallen. Information on these activities is relatively scarce, but a number of studies conducted over the years give some indication of the trends.¹ Consider private security markets, for example.

Crime rates have actually been trending down since 1980 (after fluctuating through the 1970s) except for the upturn in 1985–91, during a dramatic change in criminal-justice policy nationwide.² There were 5,950 reported crimes per 100,000 population in 1980 versus 5,175.3 in 1984.

Private security employment has accelerated since 1970. A 1970 estimate put the number of privately employed security personnel in the United States at roughly equal to the number of government, or public, police. Since then, public police employment, unlike private security employment, has not changed much. In 1990 there were roughly 2.5 private security personnel (about 1.5 million total) to every public police officer.³ This ratio is

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rapidly approaching 3 to 1, if it has not already reached that level.⁴ Thus, in 1990 an estimated \$52 billion was spent for private security services in the United States compared to about \$30 billion for federal, state, and local police.⁵

The private security market apparently is the second fastest growing industry in the United States,⁶ but increasing employment of private security personnel is only part of the story. Going back to 1970 again, a study found that the use of security equipment was increasing at about 11 percent per year,⁷ but the growth rate in expenditures on security equipment reached an estimated 15 percent in 1990 when they rose to an estimated \$17 billion.⁸

Provision of residential alarm systems (already the most frequently used component of security programs for business) provides one example of the spread of such security technology. It is estimated that at least 10 percent of the homes in the United States were connected to central alarm systems in 1990,⁹ up from one percent in 1970.¹⁰ One estimate by Leading Edge Reports suggests that total sales of central alarm station services rose by 36.9 percent (from \$5.26 million to \$7.20 million) between 1987 and 1989 (during the upsurge in the war on drugs).¹¹

While statistics are not readily available, it appears that this trend has accelerated through the 1990s. But these services are only one of many aspects of the security market that rely on technology rather than or in addition to manpower. Electronic access control equipment sales grew by an estimated 23 percent between 1987 and 1989, while increases in sales of electronic intrusion detection equipment, vehicle protection equipment, and closed-circuit television (CCTV) were 21, 44, and 25 percent respectively, and growth rates for sales of metal detectors, x-ray devices, computer security equipment, electronic article surveillance equipment, and other types of security technology are all comparable.¹²

Better Technology

It is not just numbers and expenditures that

are rising. Both increasingly sophisticated labor and capital are being combined to produce ever higher levels of security where it is demanded. The last three to four decades have witnessed dramatic changes in security technology, with the arrival of CCTV, microwave detection systems, portable radios and cameras, magnetic sensors, and laser technology, to name a few. And all these technologies are constantly being improved; devices that were on the cutting edge only a short time ago are obsolete. As a salesman explained to me, firms have to continue to improve products because thieves figure out how to circumvent security devices. Beyond that, they have to keep pace with new and vigorous competition.

Training for security personnel has had to improve dramatically to take advantage of the new technologies. Security personnel still include minimum-wage night watchmen, the stereotypical security from the 1950s and 1960s. But they also include highly trained and skilled electronic-security experts and security-design consultants, thanks to a growing demand for detection and deterrent equipment and price-cutting technological advances.

Given the demand for security and the increasing sophistication of many security personnel, it should not be surprising that entrepreneurs are discovering ways to supply a package of services that add up to more secure environments. Residential and business developments are increasingly being designed with security in mind. Enclosed malls and office complexes are attractive to businesses for many reasons, but security generally is part of the contract.

Apartments and condominiums often operate in a similar fashion. Such arrangements are apparently attractive: an estimated 24 million Americans lived in locked condominiums, apartment complexes, and cooperatives in 1997.¹³ Private residential communities, consisting of large numbers of single- and/or multiple-family homes on private streets, are increasingly being developed with security as a selling point. A 1997 estimate put the number of people in some 30,000 "gated" communities at around eight million, with a half-million in California alone.¹⁴

The Results

Studies of the consequences of private-sector crime control activities are rare, but several informative ones exist. A study done in the mid-1980s examined the activities and consequences of the private security force in Starrett City, a 153-acre complex in a high-crime area of Brooklyn, with 56 residential buildings containing 5,881 apartments and about 20,000 racially and ethnically diverse but largely middle-income residents.¹⁵ Starrett City had only 6.57 reported crimes per 1,000 population, compared to 49.86 for the 75th precinct in which Starrett City is located. This is all the more remarkable, considering that Starrett City residents are much more likely to actually report crimes to their security personnel than citizens in general are. (Victimization surveys indicate that more than 60 percent of crimes with victims go unreported.¹⁶)

Similar results appear elsewhere. For instance, one of the most intriguing cooperative privatization schemes in recent history is in St. Louis and University City, Missouri.¹⁷ In 1982 the St. Louis metropolitan area had more than 427 private street-providing organizations.¹⁸ The titles to these formerly public streets are now vested in incorporated street associations to which all property owners must belong and pay dues. The street associations, most of which own one or two blocks, have the right to close their streets to through-traffic to limit cars to those of residents and their visitors. More important, ownership gives the neighborhood a high degree of cohesiveness, and the resulting cooperative behavior produces an increased awareness of activities on the streets. That along with limited access and, in a few cases, security patrols significantly lowered crime in virtually every category relative to comparable public streets. For instance, Ames Place's crime rate was 108 percent lower than the adjacent public street.¹⁹

Smaller scale private security arrangements are also effective. Critical Intervention Services (CIS) provides private security to landlords who own apartment complexes priced to attract low-income tenants. Since CIS began offering service in Tampa, Florida, in 1991, it has received many more requests than it can

serve, but it has expanded into Miami, Jacksonville, and Orlando. Revenues grew from \$35,000 to roughly \$2 million in 1996. The firm provided security for 50 apartment complexes that year, and crime dropped by an average of 50 percent.²⁰

Private security and protection arrangements also can have a general deterrence effect. A 1996 analysis of Lojack, a hidden radio transmitter installed in cars to aid in recovery after theft, concluded that a 1 percentage point increase in installations is associated with a 20 percent decline in auto thefts in large cities and a 5 percent reduction in the rest of the state.²¹

Lojack greatly reduces the expected loss for car owners who use it, since 95 percent of the cars equipped are recovered, compared to 60 percent for cars without it. But this direct benefit is only part of the total benefit. Because a potential car thief does not know if a vehicle is protected by Lojack, its existence in a market creates uncertainty that deters auto thefts. According to the study, "Lojack appears to be one of the most cost-effective crime reduction approaches documented in the literature, providing a greater return than increased police, prisons, job programs, or early education interventions."²² A recent extensive study of concealed handguns reaches similar conclusions; violent crimes, including murder, rape, and robbery, are significantly deterred when potential criminals know that citizens may carry concealed handguns.²³

Public vs. Private Police

A comprehensive 1992 statistical study used data from 124 Standard Metropolitan Statistical Areas in an effort to analyze the effect of both public police and private security on the overall safety of communities and on decision-making by offenders.²⁴ The addition of public police showed no statistically significant deterrence, but the result of private security was significant. Additional private security personnel correlated with less crime, suggesting that the benefits spill over into the community at large.

Public police may not like this finding, but they are increasingly recognizing its validity

as they turn to "community policing" arrangements. In Chicago, for instance, the police department is implementing a massive change in its policing strategy, abandoning the "traditional" model of policing that relies on random automobile patrols, rapid response, forensic technology in after-the-crime investigations rather than citizen information, and a focus on arrest and incarceration.²⁵ The new Chicago Alternative Policing Strategy emphasizes the need for community involvement in a "proactive" effort to prevent crime. While the program is relatively new, the intentions are to help develop local citizen and business crime-watch groups and to put public police back on the beat in large part to establish cooperative relationships with the people in neighborhoods. This is what private security often does. In fact, noted criminologist Lawrence Sherman defines community policing as police acting like security guards. So another consequence of the growing private response to crime is that it is providing public police with an alternative model.²⁶

A massive 1976 report by the National Advisory Commission on Criminal Justice Standards and Goals concluded that "the private security industry . . . offers a potential for coping with crime that can not be equaled by any other remedy or approach. . . . Not represented on the boards or staffs of State Planning Agencies, rarely used by municipal or county planners, only infrequently consulted by elected officials, [this] . . . industry [has] crime prevention answers desperately needed by homes, schools, businesses, neighborhoods and communities."²⁷ Even though politicians have rarely recognized, and crime researchers are only beginning to recognize, how accurate this study's conclusion is, private citizens clearly know it already. The results are becoming increasingly apparent. They and the private entrepreneurs who respond to their demands deserve much of the credit for falling crime rates, despite the politicians' assertions that they are responsible. □

to drug crimes; fewer police were available to deter nondrug crimes, and prison crowding increased as drug criminals flowed in, forcing the early release of nondrug criminals; responses by the private sector and by legislators (for example, prison building) took time. Thus the general downward trend was not re-established until 1991. See Bruce L. Benson, Iljoong Kim, and David W. Rasmussen, "Deterrence and Public Policy: Tradeoffs in the Allocation of Police Resources," *International Review of Law & Economics*, 1998, pp. 77-100; Benson, Kim, Rasmussen, and Thomas W. Zuehlke, "Is Property Crime Caused by Drug Use or Drug Enforcement Policy?" *Applied Economics*, 1992, pp. 679-692; and Rasmussen and Benson, *The Economic Anatomy of a Drug War: Criminal Justice in the Commons* (Lanham, Md.: Rowman and Littlefield, 1994).

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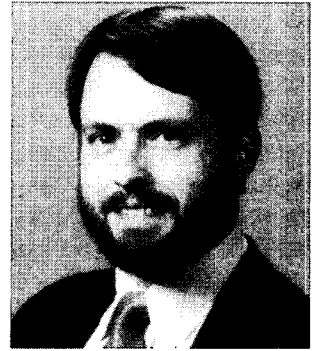
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New Excuses for Old Failures



Foreign aid, argues President Bill Clinton, is “designed to keep our soldiers out of war.” He threatened to veto this year’s \$12.7 billion foreign assistance appropriations bill after Congress reduced his request by \$2 billion. But the evidence is overwhelming that increasing foreign aid would only throw good money after bad.

The United States alone has contributed more than \$1 trillion (in current dollars) in foreign assistance since World War II. Although some individual development projects have undoubtedly worked, there is no evidence that what we inaccurately call “foreign assistance” has generated economic growth or promoted political stability in the developing world.

In 1996 the United Nations reported that 70 countries, aid recipients all, were poorer than they were in 1980; 43 were worse off than they were in 1970. Admits the U.S. Agency for International Development (U.S. AID): “much of the investment financed by U.S. AID and other donors between 1960 and 1980 has disappeared without a trace.”

The already overwhelming evidence that foreign aid is not aid just keeps accumulating.

There was, for instance, last summer’s *New York Times* exposé detailing an investigation by the Office of the High Representative in Bosnia, which concluded that as much as \$1 billion of that artificial nation’s public money

had been stolen since 1995 even as the West was providing \$5.1 billion in aid. Alexandra Stiglmyer, spokeswoman for the High Representative, said “The figure is probably higher than \$1 billion.”

To argue, as the State Department did, that the bulk of the loss was the Bosnians’ own funds ignores the fact that money is fungible and most of the economy remains under state control. It is bad enough to force Western taxpayers to subsidize local corruption. It is criminally irresponsible to make them underwrite a system that actively impedes economic development and growth.

Russian Woes

Russia is no different. Moscow has collected more than \$20 billion from the International Monetary Fund alone since 1992; the money is gone and the country is poorer than ever. Russia defaulted on billions in loans in 1998 and last August reached an agreement with Western creditors to put off repaying \$8.1 billion falling due in 1999 and 2000. A \$640 million loan issued by the IMF in July was simply shifted among Fund accounts to pay down Russia’s outstanding debt.

Even the IMF makes little pretense that its activities promote economic reform. The Fund’s Stanley Fisher admits that “we were lied to” when Russia transferred hundreds of millions of dollars of its 1992 loan to offshore accounts to speculate in Russian bonds.

There are concerns that looted IMF funds may have been laundered through the Bank of

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New York, which appears to have become a transit station for the Russian mob. But Fund officials say that they can't be expected to track the disposition of IMF disbursements: "We are not a bank," Thomas Dawson, the director of external relations, told the *Wall Street Journal*.

Nor, it would appear, is the Fund a trustworthy forecaster. A Heritage Foundation study released last August found that while the organization did a reasonably good job of assessing the economies of industrialized states, it did a lousy job of predicting events in poor nations—the ones to which it was lending. Whether the IMF shaded the truth to justify its activities or displayed a hopeless naïveté in judging the creditworthiness of its borrowers is impossible to say for certain. However, wrote William Beach, Aaron Schavey, and Isabel Isidro, the Fund's consistent failure weakened "the IMF's effectiveness because early diagnosis of its member countries' vulnerabilities to potential crises is critical to fulfilling the IMF's mandate of ensuring the international financial system's stability."

It's not just the IMF. The World Bank stood by for decades as the Suharto regime and especially his family looted the Indonesian economy. The organization finally felt compelled to hold up planned disbursements before parliamentary elections last year to prevent government manipulation of aid for political purposes and threatened to halt its entire lending program because of a banking scandal.

Also in 1999 economists Alberto Alesina and Beatrice Weder produced a shocking study for the National Bureau of Economic Research. In assessing the experience of aid from 1970 to 1996, they concluded that more assistance, whether bilateral or multilateral, tends to flow to more corrupt governments. Stephen Knack of the University of Maryland completed a survey which found that "higher aid levels erode the quality of governance, as measured by indexes of bureaucratic quality, corruption, and the rule of law."

In short, aid has proved to be a disaster. Which may explain President Clinton's attempt to come up with a new argument: foreign assistance will prevent wars. He warned that without the \$2 to \$3 billion he wants for

Kosovo and related programs, "make no mistake—there will be another bloody war."

Old Argument

It's a superficially appealing argument, but hardly new. Former U.S. AID Administrator J. Brian Atwood peddled the mission of "crisis prevention" for years. Before departing last July, he said that without more aid money "you could see more countries becoming anarchies in Africa. You certainly could see that as a possibility in Russia."

In fact, however, U.S. and international assistance has flowed freely not just to Russia, but to virtually every country that has descended into anarchy and/or war. Between 1971 and 1994 the United States, Europe, and multilateral institutions gave Sierra Leone \$1.8 billion, Liberia \$1.8 billion, Angola \$2.9 billion, Haiti \$3.1 billion, Chad \$3.3 billion, Burundi \$3.4 billion, Rwanda \$4.7 billion, Uganda \$5.8 billion, Somalia \$6.2 billion, Zaire \$8.4 billion, Mozambique \$10.5 billion, Ethiopia \$11.5 billion, and Sudan \$13.4 billion.

Aid failed to forestall crises in all of these states because money was never the basic problem. Most of these nations are riven with clan, ethnic, or tribal rivalries. Most lack a basic rule of law. Most have repressive, dishonest governments. Most suffer from highly politicized militaries.

More money from abroad would solve none of these problems. To the contrary, pouring cash into states such as Ethiopia, Somalia, Sudan, and Zaire subsidized the very worst autocratic and corrupt dictators who consciously wrecked their nations. This made chaos and war more, not less, likely. Observes Alex De Waal, onetime vice-director of Africa Watch: "The more aid a country receives, the less the government of that country has to answer to the people."

President Clinton's attempt to dress up yesterday's disastrous policies with new justifications will fail. There is perhaps no greater tragedy today than the failed societies that dot the globe. But there is no evidence that increasing aid flows will benefit Third World peoples, let alone prevent new human catastrophes. □

Technology, Progress, and Freedom

by Edward W. Younkings

Technology represents man's attempt to make life easier. Technological advances improve people's standard of living, increase leisure time, help eliminate poverty, and lead to a greater variety of products. Progress allows people more time to spend on higher level concerns such as character development, love, religion, and the perfection of one's soul.

If people resisted technological change, they would be expressing their satisfaction with existing levels of disease, hunger, and privation. In addition, without experimentation and change, human existence would be boring; human fulfillment is dependent on novelty, surprise, and creativity.

An innovative idea from one man not only contributes to the progress of others, but also creates conditions permitting people to advance even further. Ideas interact in unexpected ways, and innovations are frequently used in unforeseen applications. Technological progress involves a series of stages consisting of experimentation, competition, errors, and feedback.

Innovations do not simply replace other products. Rather, they develop new and expanded markets of their own. New technology does not cause a net increase in unemployment or make labor obsolete. While technology eliminates some jobs, it is a net creator of jobs because resulting higher profits are

reinvested. New technology may require the development of new skills and the need to relocate, but it does not cause greater overall unemployment. As technological improvements increase productivity, the demand for labor will tend to rise, creating more job opportunities and raising wages. The increase in labor productivity also raises the potential of some unemployed workers, whose marginal costs previously exceeded their marginal productivity. Finally, as consumers, wage earners will gain from the decrease in product prices that tends to result from the increase in productivity and output.

Freedom Promotes Technological Progress

There is a reciprocal relationship between technology and freedom. A free market unhampered by government intervention is the most fertile environment for technological and economic progress. Freedom is a prerequisite for progress in an unpredictable and risky world. It encourages profit-seeking and innovation, which in turn result in greater productivity and employment. Technology furthers a free society by providing new opportunities to communicate, work, compete, and deal with others across social and physical barriers. In the past, the wheel and the steam engine enhanced and complemented human physical powers. Today, innovations such as the microprocessor amplify human intellectual capabilities. The electric motor, internal

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combustion engine, fluorescent and incandescent lighting, and the Internet have had enormous effects on the way we live and work. Emerging technologies such as cryogenics, photovoltaics, aerogels, fuel cells, and radio-wave lighting may do the same in the future.

When legislators pass laws that restrict or forbid the use of technology, they grant a privilege to stagnant firms and their workers at the expense of the firms that would have used the new technology and the workers who would have had different, often better jobs. Resources remain in inefficient protected technological processes, creating waste and impeding progress.

Calls for protectionism come from firms that have not modernized their production processes and thus are unable to compete with more efficient, lower-cost companies. Both mandated compensation to displaced laborers and restrictions on the use of technology will reduce the profits of the firms affected, thereby reducing capital accumulation and its reinvestment that would have led to an eventual increase in the level of employment.

Friends and Enemies of Progress

Virginia Postrel's 1998 book, *The Future and Its Enemies*, defies conventional political boundaries of left and right and liberal and conservative to divide the world into dynamists and stasists. The book's thesis is that the most useful and pertinent intellectual concept is about those who welcome the future and those who want to stop, turn back, or regulate change.

According to Postrel, dynamists prefer an open-ended society where creativity and enterprise, operating under general and predictable rules, generate progress in unpredictable ways. Dynamists appreciate evolutionary processes such as market competition, playful experimentation, scientific inquiry, and technological innovation. They work creatively across barriers and obstacles and in areas once thought to be disparate to construct combinations based on the free play of imagination and discovery. Further, they seek progress, rather than perfection, through trial

and error, feedback loops, incremental improvement, diversity, and choice. They are learners, experimenters, risk takers, and entrepreneurs who understand the importance of local knowledge and evolved solutions to complex problems. Not surprisingly, dynamists are frequently attracted to biological metaphors as symbols of unpredictable change and growth, variety, experimentation, feedback, and adaptation.

Stasists have an aversion to change and either abhor progress or want to control it according to their own vision. They include those who long for the good old days, technophobes, technocrats, supporters of big government programs, and individuals whose investments or jobs are in jeopardy due to some innovation. They may come from the "left" (unionists, environmentalists, Luddites) or from the "right" (traditionalists, nativists). Stasists on the left want to regulate the market and the development of technology. Those on the right loathe change and have protectionist economic leanings.

Of course, not all change is for the good. The desirability of a given change is subject to rational assessment. What is required is a libertarian institutional framework that guarantees man the freedom to seek his material and moral well-being as long as he does not infringe the equivalent rights of others. Only then will a person be able to use his rationality and free will to choose, create, and integrate all the values, virtues, and goods that can lead to individual well-being. This naturally includes the rational evaluation, choice, and use of technology and innovations.

Privatizing Federal Research and Development

Science and technology fare better under free markets than under central planning. The individual is better than the government at gaining knowledge, and the system of private property and private enterprise is able to reward human ingenuity. There is no evidence that innovations come from government bureaucracies, but entrepreneurs can often accomplish what government planners say can't be done.

Since the engine of innovation and produc-

tivity is investment in the private sector, it follows that we should favor an economic climate that rewards private investment in research and development and promotes the effective and innovative use of technology by private firms.

We need to reallocate the responsibility for technological innovation away from the state and into the hands of private technology makers and consumers. Currently, some 700 scientific and technological research labs are owned or supported by the federal government. Recently, they have expanded their scope beyond basic R & D to provide services that compete with private-sector scientific, testing, and energy firms. Privatization would end subsidies to major industries (such as petroleum and aerospace). It would also free labs from the constraints of the federal budget process, cumbersome procurement and civil service rules, and the inability to sell their services at market prices.

Advocates of federal research funding argue that the private sector will do too little because of market failures resulting from firms' free riding on others' research. Consequently, the argument goes, there will be an underinvestment in R & D.

There is no evidence that government will triumph or that markets will fail. In the public sector, research funds are awarded on political grounds; it's a form of pork-barrel spending. Politicians, facing the impossible job of assigning priorities to a myriad of research projects, tend to choose those with the greatest number of supporters or those helping their local constituencies. On the other hand, private-sector scientists and entrepreneurs are guided by price signals and choose research projects that, if successful, would be the most profitable and the most likely to meet human needs. Markets and price signals permit superior targeting of research projects and resources, and private firms can earn large rewards by solving important problems. In addition, the private sector's superior ability to select and use R & D resources will increase technological progress over the years.

Privatization is overdue for federal research

facilities. The task of linking research with human needs is not suitable for a political bureaucracy. That's why the private sector hasn't been much interested in what the federal labs create.

Reducing Federal Technology Transfer Activities

With the passage of the Stevenson-Wydler Innovation Act of 1980 and the Federal Technology Transfer Act of 1986, all Federal labs were required to develop programs for transferring technology to the private sector and to state and local governments. President Reagan supported the second act because he believed that investments in R & D for federal programs were not returning sufficient dividends to taxpayers in terms of new products, processes, and jobs. This legislation was amended in 1996 by Public Law 104-113, which created incentives and encouraged the commercialization of technology created in federal labs. A National Technology Transfer Center (NTTC) was established in 1989 by Congress to provide American firms and individuals with access to federal R & D to better enable them to compete in the international marketplace. In addition, the government, rather redundantly, has six Regional Technology Transfer Centers (RTTC's) to help U.S. firms improve their competitiveness by assisting them in the location, assessment, acquisition, and utilization of technologies and scientific and engineering expertise within the federal government.

The use of federal R & D results has been meager; studies indicate that only about 10 percent of federally owned patents have ever been used. This is unsurprising. Since R & D in federal labs is undertaken to meet an agency's mission, decisions reflect political rather than commercial needs.

Ultimately, the privatization of federal labs will transfer resources out of the hands of statist government bureaucrats, technology transfer agents, and scientists and into the hands of private-sector dynamists who are more likely to foster economic prosperity, technological progress, and cultural innovation. □



Remembering Krafft-Ebing

In my previous column (November 1999), I showed that mental illness is not a disease because it does not meet the scientific criterion of disease. In this column I will show that the primary purpose of psychiatry is not medical-therapeutic because its historical mandate and primary purpose is not to remedy a patient's diseases but to soothe society's conscience about its attitude toward unwanted persons.

In large part because of Freud's influence, people now view psychiatry as a medical specialty devoted to helping persons suffering from mental illnesses. This is an error. Before psychiatry was called "psychiatry," it was called "mad-doctoring" and its aim was to protect society from dangerous and troublesome madmen and madwomen. Today, psychiatrists perform two mutually antagonistic functions: they help society (involuntary psychiatry) and they help patients (voluntary psychiatry). However, these functions are typically confused and intermingled, with the result that helping society—even if doing so harms the patient—is also defined as a "treatment." The situation was much clearer a hundred years ago.

Psychopathia Sexualis

Sex was a hot subject in fin-de-siècle Europe and perhaps nowhere else more so

than in Vienna. Contrary to popular knowledge, the most famous expert on sex in those days was not Sigmund Freud, but Richard von Krafft-Ebing (1840–1902), whose enduring fame rests on his book *Psychopathia Sexualis*, first published in 1886. This work went through numerous editions in German and became an international best seller. Especially in retrospect, it is obvious why this book became so vastly popular: It was the first modern pornographic tract successfully merchandised as medical science, a feat accomplished largely by larding the text with Latin words. Given that in those days most educated people had a working knowledge of Latin, this must have made the book all the more titillating. There is indirect evidence for this assumption: In the Preface to the Twelfth Edition of *Psychopathia Sexualis*, Krafft-Ebing explained: "The number of technical terms has been increased, and the Latin language is more frequently made use of than in the former editions." The medical mask succeeded in transforming the voyeurism to which Krafft-Ebing was pandering from sexual perversion into scientific compassion.

The technique worked like a charm. The public continued to devour this nonpictorial precursor to *Playboy*. This was not surprising. For the first time in history, *Psychopathia Sexualis* offered people a catalogue of the countless ways—other than the missionary position in heterosexual intercourse—in which human beings could extract sexual pleasure from their bodies. Prior to the publication of *Psychopathia Sexualis*, abnormal sexual acts

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were, literally, “unspeakable abominations,” shoved under the carpet of human consciousness as bestial, unnatural, and sinful, and of course criminal as well. This meant that the law, and hence society, could not turn its back on what were then—in a telling conflation of sin and sickness—called “perversions.”

I can here provide the reader only with a small sample of the wares offered in this 617-page tome. Masturbation was, of course, high on Krafft-Ebing’s list of perversions, as it was also on Freud’s. He declared: “Nothing is so prone to contaminate—under certain circumstances, even to exhaust—the source of all noble and ideal sentiments, which arise of themselves from normally developing sexual instinct, as the practice of masturbation in early years.” Homosexuality also came in for its share of attention.

And so it went, offering the reader a manual on how to perform perversions, acts that, for the most part, have since been “discovered” to be basic human rights.

The Method in Mad-Doctoring

Shakespeare said there is “method in madness.” He meant that madness—say, such as Lady Macbeth’s—had meaning and purpose, attributes we cannot attach to a disease, such as gout. There was method in mad-doctoring as well, and Krafft-Ebing told us what it is. “The object of this treatise [*Psychopathia Sexualis*],” he wrote in the Preface to the First Edition, “is merely to record the various psychopathological manifestations of sexual life in man and to reduce them to their lawful conditions.” Krafft-Ebing did not *record* “psychopathological manifestations”; he *named* certain forbidden behaviors “psychopathological manifestations.”

Why did he do so? He told us: “The *medical barrister* only then finds out how sad the lack of our knowledge is in the domain of sexuality when he is called upon to express an opinion as to the *responsibility of the accused* whose life, liberty, and honor are at stake” (emphasis added). Krafft-Ebing identified his role as that of medical barrister. He did not pretend to make a bona fide diagnosis, much less claim to treat a patient.

But if an act is defined as a crime, and if a person commits that act, is caught, and is brought to trial for it, what is or ought to be the role of a physician in the adjudication of that person’s guilt or innocence? Obviously, the answer hinges on whether the act is perceived and defined as *caused*, partly or wholly, by a disease from which the defendant suffers. If the act is viewed as having nothing to do with disease—and there are few acts still so viewed today, but bank robbery will do as an example—then, clearly, doctors have no rational role in the trial. On the other hand, if the act is viewed as being a direct manifestation or “product” of a disease—the “meaningless” violence of a “diagnosed schizophrenic” is an example—then, as we now see it, doctors have a decisive role to play in the trial. One of the main architects of this modern—ostensibly scientific, but actually pseudoscientific—perception was Krafft-Ebing. He declared: “It is the sad privilege of medicine, and especially of psychiatry, to ever witness the weaknesses of human nature and reverse side of life. The physician finds, perhaps, a (satisfaction) solace in the fact that he may at times *refer those manifestations which offend against our ethical or aesthetical principles to a diseased condition of the mind or the body*. He can save the honor of humanity in the forum of morality, and the honor of the individual before the judge and his fellow-men. It is from the search of truth that the exalted duties and *rights of medical science* emanate” (emphasis added).

Res ipsa loquitur. The thing speaks for itself. Krafft-Ebing candidly acknowledged that the basic aim of institutional psychiatry is moral and legal, not medical or therapeutic. I claim no originality for this opinion, only the courage to express it in America at the dawn of the 21st century. Karl Kraus (1874–1936), the famed Viennese satirist, said it all: “The donkeys [psychiatrists] are led in, see through the accused, and say yeah just as the prosecutor wants them to. However, inasmuch as psychiatrists call their task . . . ‘disposition of difficult cases,’ they do not consider themselves stupid asses. Thus, they invite comparison with a more intelligent species of domestic animal: Our loyal psychiatrists are rather like good dogs—they protect house and yard.” □

William E. Rappard: An International Man in an Age of Nationalism

by Richard M. Ebeling

On April 1, 1947, 35 free-market economists, political scientists, philosophers, journalists, and businessmen met at the Swiss Alpine resort of Mont Pèlerin. They had been brought together by F. A. Hayek to found a society of classical liberals devoted to the restatement and defense of the principles of the free society. Among the attendees were Milton Friedman, F. A. Harper, Henry Hazlitt, Frank H. Knight, Ludwig von Mises, Michael Polanyi, Karl Popper, FEE President Leonard E. Read, Lionel Robbins, Wilhelm Röpke, and George Stigler.

The opening address was delivered by William E. Rappard, co-founder and director of the Graduate Institute of International Studies in Geneva, Switzerland. After welcoming the participants he reminded them that “economics” can be viewed either as a science concerned with objectively explaining how the market functions or as a policy that, based on scientific insights, proposes how men may more effectively arrange their social relationships to improve their circumstances. Rappard emphasized that:

Science cannot be liberal or illiberal.
In a sense it cannot be anything but liber-

al. An economist as a scholar may be learned or ignorant, intelligent or dull, profound or superficial, but he cannot be liberal or illiberal. Rather, if he is illiberal as a man of science, that is, if he dogmatically and intolerantly denies the rights of liberty of thought without which there can be no true science, then he is not worthy of being called a man of science. Policies can however be liberal or illiberal. Most policies all over the world today are in fact illiberal and it is because we believe that they should be liberal that we are assembled here today. It is as economists in the second sense of that equivocal word that we are liberal. Or rather we are liberals by conviction, by faith, while most of us are by profession scientific economists.

The contemporary world had turned its back on the classical liberal, free-market alternative in favor of socialism, interventionism, and welfare statism. It was to begin “an intellectual, economic and political renaissance” for liberty that the Mont Pelerin Society was being founded, Rappard said. Because, he continued, “Unless the world has become completely mad, it must sooner or later come to realize and to admit the productive superiority of a society based on the principle of free enterprise.”¹

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The years between the two world wars were a dark time for the advocates of individual liberty, free markets, and limited government. The dominant ideologies had been socialism, communism, fascism, national socialism, interventionism, and political and economic nationalism—in short, practically every imaginable form of collectivism.

The voices that spoke out against this trend were few. Among them, and one of the most articulate and influential, was that of William E. Rappard. He was an international man in an age of collectivism and nationalism, speaking in defense of global peace, free trade, and human freedom. His long-time friend and former colleague Ludwig von Mises considered him one of “the world’s foremost experts in the field of international political and economic relations.” Mises called Rappard’s 1938 book, *The Crisis of Democracy*, “the most powerful refutation of the doctrines of Communism and Nazism. There are but few authors whose judgment, competence, and impartiality enjoy a prestige equal to that of Rappard.”² And Lionel Robbins, professor at the London School of Economics, considered Rappard to be “one of the truly great men of the interwar period.”³

Born in New York

William Emmanuel Rappard was born in New York City on April 22, 1883, of Swiss parents, his father working in the United States as a representative of various Swiss industries.⁴ William Rappard did his graduate studies in economics at Harvard University from 1906 to 1908. During the academic year 1908–1909 he did additional study at the University of Vienna in Austria-Hungary, attending the seminars of Eugen von Böhm-Bawerk and Eugen Philippovich von Philippsberg, two of the leading figures of the Austrian school of economics before the First World War. And from 1911 to 1913, he was an adjunct professor of political economy at Harvard.

In 1913 he was appointed professor of economic history and public finance at the University of Geneva in Switzerland. He also served as rector of the University of Geneva during 1926–1928 and 1936–1938. From

1917 to 1919, Rappard was a member of various Swiss diplomatic missions to Washington, D. C., London, and Paris, including service with the Swiss delegation to the peace conference in France that ended the First World War. He made a strong impression on President Woodrow Wilson and was highly influential in persuading him to choose Geneva as headquarters of the League of Nations beginning in 1920.

From 1920 to 1925 he was the director of the Mandates Division of the League for overseeing the administration of colonial territories lost by the Central Powers at the end of the war, and was a member of the Permanent Mandates Commission of the League from 1925 to 1939. From 1928 to 1939 he also served as a member of the Swiss delegation to the annual meetings of the League’s General Assembly.

But in the struggle for classical-liberal and free-trade ideals, Rappard’s greatest institutional contribution between the world wars was his co-founding in 1927 of the Graduate Institute for International Studies in Geneva, with Paul Mantoux, the internationally respected economic historian and expert on the industrial revolution. Rappard’s goal was to offer to international students “the most eminent specialists available. If these specialists are well chosen, not only for their intelligence and erudition, but also for their character, and if they are made to realize that their sole professional duty is to contribute to the progress of science through their own work,” then the Institute would have done all that it could to train a new generation of scholars and advance the cause of peace and freedom.⁵ Throughout the 1930s the Institute’s financial status was secured by the generosity of the Rockefeller Foundation.

Among the teaching staff at the Graduate Institute in the 1930s, along with Rappard and Mantoux, were Maurice Bourquin, professor of diplomatic history; Guglielmo Ferrero, professor of contemporary history; Michael A. Heilperin, professor of international monetary relations; Hans Kelsen, professor of international law; Mises, professor of international economic relations; Pitman Potter, professor of international political relations; and

Wilhelm Röpke, professor of international economic relations. Each was internationally renowned as a leading contributor to his respective discipline, and several had found sanctuary at the Graduate Institute as exiles from Nazism and fascism in their own homelands.

Hosted Visiting Scholars

Rappard also brought to Geneva during these years an array of famous visiting scholars, many of them leading classical liberals, who would deliver lectures over a week; their lectures often were sponsored for publication by the Graduate Institute.⁶ Among those visitors were Röpke (before he joined the Institute's staff), F. A. Hayek, Lionel Robbins, Louis Rougier, Quincy Wright, Luigi Einaudi, Eric Voegelin, Fritz Machlup, Gottfried Haberler, and Bertil Ohlin.⁷

The Institute also held a lecture program every summer from 1927 to 1939 on the topic of international peace and order. The lectures were published in an annual series under the title *Problems of Peace*. In 1938, to mark the Institute's tenth anniversary, Rappard edited a collection of essays by the Institute's faculty on the theme of *The World Crisis*, through which the world was then passing.⁸

In September 1939, days after the beginning of the Second World War in Europe, Robbins recalled his last visit to the Graduate Institute as a guest lecturer and said nostalgically: "How much of all that was most stimulating and inspiring in the period between the wars is typified in their lovely college by the lake. Long may it flourish, an oasis of sanity in a mad world, to preserve and advance the great principles of international citizenship for which it so conspicuously stands."⁹ The Graduate Institute survived the war and continued to flourish after 1945, with Rappard as its director until his retirement in 1955. He died on April 29, 1958, a few days after his 75th birthday.

Three Themes

Throughout the interwar period Rappard's writings focused on what he argued were

three interdependent themes: (1) international order and collective security as represented by the League of Nations; (2) free trade and private commerce to depoliticize economic relationships and reduce international tensions; and (3) respect for the dignity of the individual and protection of his rights to liberty and property to assure a free and just society.

After the disillusionment with and failures of the League of Nations, Rappard's fervent defense and support of it in the 1920s and 1930s may seem peculiar and misplaced in the context of more recent classical-liberal and conservative criticisms of concentrated power in international organizations. But it needs to be appreciated that in the nineteenth and twentieth centuries many if not most of the free-market liberals considered private commerce and free trade as essential not only for enhancing the wealth of nations but for fostering peace by reducing to the minimum the intervention of governments in human intercourse.

As an extension of this, they also considered treaties and agreements among governments for the uniformity of law and contract to be essential for international trade and commerce. They believed that an international court to adjudicate disputes between nations would reduce the likelihood of war. And to prevent war some supported an international system of collective security, composed of a consortium of nations' military power, to provide mutual defense against would-be aggressors.¹⁰

Even as principled an advocate of *laissez faire* and strictly limited government as Ludwig von Mises said in 1927 that "The [classical] liberal therefore demands that the political organization of society be extended until it reaches its culmination in a world state that unites all nations on an equal basis. For this reason he sees the law of each nation as subordinate to international law, and that is why he demands supranational tribunals and administrative authorities to assure peace among nations in the same way that the judicial and executive organs within each country are charged with the maintenance of peace within its own territory." And he offered the hope that "a world super state really deserving

of the name may some day be able to develop that would be capable of assuring the nations the peace that they require.”¹¹

Rappard wrote four books on the ideal, the practice, and the failure of the League of Nations.¹² These were supplemented by various articles on the workings and reality of the League.¹³

Swiss Model

Rappard’s model of international organization for world peace was based on his analysis of the evolution of collective security in the Swiss confederation.¹⁴ Starting in the thirteenth and fourteenth centuries, a coalition of independent states in the Swiss Alps began to be formed for mutual military assistance against external threats. It eventually incorporated most of the territory now known as Switzerland. The common policy was strict neutrality and noninterference in the affairs of surrounding countries (though many individual Swiss soldiers sold their military services to other governments in Europe). Switzerland was invaded and conquered by Napoleon in 1798. After the defeat of France by the Allied nations, Swiss independence and neutrality were once again recognized by the European powers. In 1848 a new federal constitution was established in Switzerland that was modeled after the U.S. Constitution, with two legislative chambers but no presidency because of the people’s suspicion of any concentration of power in one person’s hands.¹⁵

The Swiss federal authority had responsibility only for national defense and neutrality-based foreign policy issues. All other matters were strictly left up to the respective cantons and to the private citizens. The constitution was also imbued with the spirit of classical liberalism and economic freedom. “Freedom of trade, residence, conscience and worship, of the press, of association and of petition were guaranteed for all. . . . [A]ll forms of protectionism were condemned as being contrary . . . to the fundamental principle of equality before the law,” Rappard explained.¹⁶

The danger from concentration of federal power manifested itself, however, with the growth in socialist and interventionist ideas in

the second half of the nineteenth century. In the 1874 revisions to the Swiss constitution the federal government was given socialist and welfare-statist responsibilities over both the cantons and individual citizens; those powers had increasingly come to threaten the liberty of the Swiss people. In 1936 Rappard expressed concern that what was developing was a form of “state socialism” and wondered if Switzerland was not on a road to serfdom: “How much further this economic anti-liberalism can be carried without seriously threatening the political liberalism to which the Swiss people are still firmly attached, is the great problem of the future.”¹⁷

In Rappard’s eyes, the League of Nations was meant to serve as an association of the countries of the world for purposes of mutual defense against violators of international peace, whether or not the aggressor was a member. The internal affairs of the member states were not subject to interference from the other members, though the hope was that those nations not yet wholly guided in their home policies by allegiance to liberty, property, and free enterprise would eventually see the benefits of establishing a regime of domestic freedom.

The peace treaty of 1919 that ended World War I had included the covenant that established the League of Nations. The new organization was assigned three primary tasks: (1) implementation of the terms of peace; (2) establishment of a system of justice through an international court to adjudicate disputes between nations; and (3) formation of an association for collective security to maintain the peace if one or more nations violated the territory and freedom of any of the member countries.

What was a new and important principle in the peace treaty, Rappard argued, was the insistence that no people may be ruled without their consent. This was reflected in the ideal of self-determination, under which individuals within geographical areas in Europe could determine through plebiscite whether they would be citizens of one nation rather than another or form their own independent national entity. In the case of Germany’s former African and Asian colonies this meant not

outright annexation of these territories by one of the victorious powers, but supervision and oversight by the League of how they were administrated as a "mandate" by one of the victorious powers. The goal was to assure the rights of the people in these territories and possibly their eventual independence rather than permanent colonial control.¹⁸

The idea behind an international court of justice was that no claimant in a dispute was capable of objectively judging his own case. Instead, a court of internationally selected and respected judges would sit in the Hague in Holland, and member states of the League would obligate themselves to present their claims against and disputes with other countries before this judicial body and accept its decisions as binding. International law and justice would replace the costs and catastrophe of war in the settling of potential global conflicts.

Finally, the members would agree to support politically, militarily, and financially any necessary armed resistance that the League as a body might agree was required to repel and defeat an attack on one of the member states by an aggressor nation that had initiated international violence. The hope was that the threat of such collective resistance would serve as a deterrent against any nation contemplating disruption of the international peace.

The ideal for which Rappard argued was a world of peace, freedom, law, and order. The League was not and had not been planned to be a world government. For many classical liberals like William Rappard, the logical extension of limited national government was to develop the practice of international justice under law, the adjudication of national disputes before an international court, and an international policing against war and violence between nations.

A Different Reality

That was one version of the classical-liberal ideal. The reality was very different. Rappard was a dispassionate recorder of the League in practice. In violation of the peace concepts of 1919, governments either manipulated or prevented self-determination for

peoples through plebiscites. They refused to recognize or respect decisions made by the international court at the Hague; indeed, governments tried to manipulate the selection of judges appointed to serve their national purposes. They filled League commissions, bureaus, and departments with members of their national bureaucracies both as a spoils system and to influence League activities. In the League's General Assembly and ruling Council, governments instructed their representatives to vote in the service of their respective "national interests" rather than for the protection and improvement of an international order of freedom, justice, and peace. And finally, in the 1930s when imperial Japan, fascist Italy, and Nazi Germany began to violate international treaties and law through war, conquest, and annexation, the League members chose to follow not the idea of collective security, but policies of national armament and defense.¹⁹

Why had so many nations turned their backs on the potential and possibility for a classical-liberal world of freedom and peace? Rappard tried to answer this in three insightful monographs and a book, the latter originally delivered as a series of lectures at the University of Chicago.²⁰

After the disruptions, dislocations, and destruction of World War I, the countries of the world had participated in numerous conferences in the 1920s and early 1930s at which it was pointed out that permanent economic stability and improved material prosperity could only be assured through renewed free trade, more open immigration, a safe environment for global private investment, and stable foreign exchange rates linked to gold. Instead the nations of the world practiced "super-protectionism," with high tariffs, import quotas, export restrictions, foreign-exchange manipulations and controls, agricultural and industrial subsidies, redistributive welfare schemes, and domestic planning, often with the goal of creating national economic self-sufficiency. While governments may have given lip service to the ideal of economic liberalism, what they all practiced was in fact economic nationalism. Rappard explained this idea and policy:

Economic and political nationalism . . . are, however, so closely related one to the other that we can in no case avoid the necessity of defining the latter if we wish to fully understand the former. Nationalism, then, is the doctrine which places the nation at the top of the scale of political values, that is above the three rival values of the individual, of regional units and of the international community. . . . If we wished to define economic nationalism by its underlying purpose, we should say that it was a doctrine destined to serve the nation by making it not richer, but freer, by promoting not its material welfare, but its independence of foreign influences. Economic nationalism is the policy of national self-sufficiency.²¹

While Rappard pointed out the most extreme forms of economic nationalism were practiced in fascist Italy and Nazi Germany, it was the dominant economic policy in all the Western democracies as well. During the First World War, governments had introduced economic planning in the name of the war effort, gaining control or influence over many aspects of commercial and social life previously viewed as the exclusive domain of private choice, association, and enterprise. After the war, many groups desired intervention and planning in peace time; some because they thirsted after the ideal of social engineering, others because they wished their vested interests to be politically protected in the changed environment of the postwar period. Still others expected government to guarantee or provide employment and business profits or market shares. After the start of the Great Depression in 1929, the pressures and appeals for such policies only increased. It was said that the various forms of national intervention needed to be isolated from international market forces that otherwise might undermine them, an isolation for which the weapons of economic nationalism were applied.

Tool of Economic Warfare

In addition, the experience of the last war and the fear of a new war generated a general



William E. Rappard

climate of political insecurity in which governments built up not only their military armaments but also their tools of economic warfare to assure domestic supplies of raw materials, agricultural produce, industrial commodities for military preparedness, and artificially manufactured substitutes for goods that might not be available during times of international conflict. "By economic armaments," said Rappard, "we mean all those legislative and administrative devices intended to restrict imports and to develop domestic production with a view of reducing international interdependence. Economic armaments are the tools of economic nationalism."²²

Rappard tried to explain how this shift from economic liberalism to paternalistic government and economic nationalism had come about. He gave a concise answer in a lecture he delivered in the United States in 1936. After citing the individualist and antistatist rationale for the American and French revolutions and the political evolution of England, he noted:

In the latter half of the nineteenth century and up to the present day, the individual, having emancipated himself from the state and having subjected the state to his will [through the democratic process], has furthermore demanded of the state that it serve his material needs. Thereby he has complicated the machinery of the state to such a degree that he has again fallen under subjection to it and has been threatened with losing control over it. . . . [T]he individual has increasingly demanded of the state services which the state is willing to render. Thereby, however, he has been led to return to the state an authority over himself which it was the main purpose of the revolutions in the beginning of the nineteenth century to shake and break.²³

Preserving the liberty that men still had and regaining the liberty that men had already lost was possible, Rappard argued, only with a reversal of state control over economic affairs through a return to economic liberalism, and with it a reduction in the powers and responsibilities of the state:

As we see it, the defense of democracy demands a return to greater economic freedom, without which no state, however organized, can give its citizens more than the illusion of governing themselves. . . . It is, therefore, not only because we believe private enterprise to be more creative, more progressive, more efficient, and consequently more productive of greater general prosperity than that of the state, that we venture to advocate a limitation of the latter. It is also because we believe that no state that has been allowed to become totalitarian in its activities can fail to become totalitarian in its claim on the subservience of its subjects. Our plea for more private liberty is, therefore, political no less than economic.²⁴

For Rappard, the calamity of the Second World War was the inevitable outcome of the collectivist, nationalist, and socialist tendencies set loose during the First World War and that reached their apex in the 1930s. What

hope, then, did he have for the world that emerged from the second “Great War” of the twentieth century?

Dubious about the U.N.

In the immediate aftermath of the war, during a visit to the United States, he delivered a series of lectures in which he expressed little confidence in the new United Nations that had superseded the old League of Nations.²⁵ Rappard argued that the United Nations was the product of a “victors’ peace.” It was designed and brought into existence by the United States, Great Britain, and the Soviet Union before the war had even ended, and was controlled and dominated by them. The initial membership was restricted to those nations who had allied themselves with the Big Three in the war, and excluded neutral countries like Switzerland. The U.N.’s real power resided in the Security Council, in which five governments—the United States, the Soviet Union, Great Britain, France, and China—not only determined when and how military force would be used against the other nations of the world, but in which each also had a veto power that prevented any U.N. sanctions and actions against themselves. Any decision on which the Big Five could agree could be virtually imposed on the other members of the United Nations. It was an organization constructed for these five powers to be the masters of the postwar world.

In 1954 Rappard delivered a lecture in which he reviewed the attempt for global peace since the end of the First World War.²⁶ In the post-World War II period, he said, global peace through the U.N. had been impossible not only because of the Big Five monopoly, but also because the two leading powers—the United States and the Soviet Union—held radically different conceptions of the meaning of “freedom,” “justice,” “self-determination,” and “peace.” Peace had depended on the two military alliances surrounding the United States and the Soviet Union. The worst fear was that a war would break out between these two camps, resulting in a nuclear calamity far more terrible than the other world wars of the century.

What was Rappard's hope for the long run? He believed that eventually the Soviet Union would collapse from internal forces. He argued that however meager living standards may be under socialist planning compared to the West, any improvement would stimulate the Russian people to want an improvement in their political status as well:

[M]ay we not hope that, as they [Soviet people] become less indigent, they will become less subservient? And as they become more impatient of police rule and of censorship, may they not grow more skeptical about the myths on which their ignorance has heretofore been fed about the West, about its exploitation of the masses, about capitalism, and about its necessarily aggressive imperialism? . . . But even if it be deemed unlikely, it seems to me that the policy of the West should not dismiss it as necessarily untrue. Nothing is to be gained by acting as if the masters of the East were omniscient in declaring war to be inevitable and everything would be assuredly lost if we let ourselves be persuaded that they were as infallible as they are dogmatic.²⁷

But besides any eventual internal collapse of communism in the Soviet Union, the West had to have its own ideal. In his last book, *The Secret of American Prosperity*, Rappard tried to explain to his fellow Europeans the lessons to be learned from the United States without forfeiting their own traditions and cultural contributions to the world.²⁸ What underlay America's technological superiority and productive strength, he said, was its spirit of free and open competitive enterprise, which created the innovations and material achievements that were the envy of the world. The secret of America's success was human liberty, Rappard emphasized. The ideal of liberty had originally come to America from Europe. Europe now needed to relearn some of that lesson from America. If it did, a world of freedom, free trade, peace, and prosperity could become a reality, rather than only the classical-liberal ideal. □

1. William E. Rappard, "Address at the Opening Meeting [of the Mont Pelerin Society] on Tuesday, April 1st, 1947."

2. Ludwig von Mises, "The Secret of American Prosperity" [1955], in Bettina Bien Greaves, ed., *Economic Freedom and Interventionism: An Anthology of Articles and Essays by Ludwig von Mises* (Irvington-on-Hudson, N.Y.: Foundation for Economic Education, 1990), p. 163.

3. Lord (Lionel) Robbins, *Autobiography of an Economist* (New York: St. Martin's Press, 1971), p. 159.

4. The following brief summary of Rappard's professional life draws from Albert Picot, *Portrait de William Rappard* (Paris: Editions de la Baconnière, 1963) and Victor Monnier, *William E. Rappard: Défenseur des Libertés, Serviteur de Son Pays et de la Communauté Internationale* (Geneva: Edition Slatkine, 1995).

5. Monnier, pp. 489–90.

6. On the history of the Institute, see *HEI: Quarantième Anniversaire, 1927–1967* (Geneva: Institut Universitaire de Hautes Etudes Internationales, 1967) and *HEI, 50: 1927–1977* (Geneva: Institut Universitaire de Hautes Etudes Internationales, 1977).

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8. William E. Rappard, ed., *The World Crisis* (London: Longmans, Green, 1938).

9. Robbins, *The Economic Causes of War*, p. 9.

10. See Edmund Sillner, *The Problem of War in Nineteenth Century Economic Thought* (Princeton: Princeton University Press, 1946); also, my article "World Peace, International Order and Classical Liberalism," *International Journal of World Peace*, December 1995, pp. 47–68.

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14. William E. Rappard, "Switzerland and Collective Security," Pts. I & II, *The New Commonwealth Quarterly*, March and June 1936, pp. 299–320, 53–64; and, *Collective Security in Swiss Experience, 1291–1948* (London: George Allen & Unwin, 1948).

15. William E. Rappard, "Pennsylvania and Switzerland: The American Origins of the Swiss Constitution" [1940], reprinted in *Varia Politica: Publiés Réimprimés à L'occasion du Soixante-dixième Anniversaire de William E. Rappard* (Zurich: Editions Polygraphiques, 1953), pp. 316–38.

16. William E. Rappard, "Switzerland and Democracy," *Fortnightly Review*, September 1937, p. 297.

17. William E. Rappard, *The Government of Switzerland* (New York: D. Van Nostrand, 1936), p. 123. Rappard was more optimistic about Switzerland's future after the Second World War. See his article "The Economic Position of Switzerland," *Lloyd's Bank Review*,

December 1948, p. 32: "Still it would seem as if, in the struggle between liberty and equality which is going on all over the world, liberty were holding its own more successfully at the foot of the Alps than in most if not all other European states. In the sphere of economic policy, this makes for a larger measure of liberalism and for a stronger opposition to state control."

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19. William E. Rappard, "Why Peace Failed," *The Annals of the American Academy of Political and Social Science*, July 1940, pp. 1–6.

20. William E. Rappard, "The Common Menace of Economic and Military Armaments" [1936], reprinted in *Varia Politica*, pp. 76–100; "Economic Nationalism" in *Authority and the Individual: Harvard Tercentenary Conference of Arts and Science* (Cambridge, Mass.: Harvard University Press, 1937), pp. 74–112; *Post-War Efforts for Freer Trade* (Geneva: Geneva Research Centre, 1938); and *The Crisis of Democracy* (Chicago: University of Chicago Press,

1938). "The Common Menace" and *Post-War Efforts* were delivered as Richard Cobden Lectures in London in, respectively, 1936 and 1938.

21. Rappard, "Economic Nationalism," pp. 78, 83–84.

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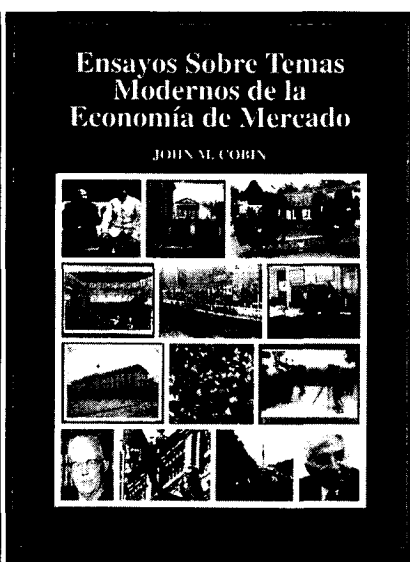
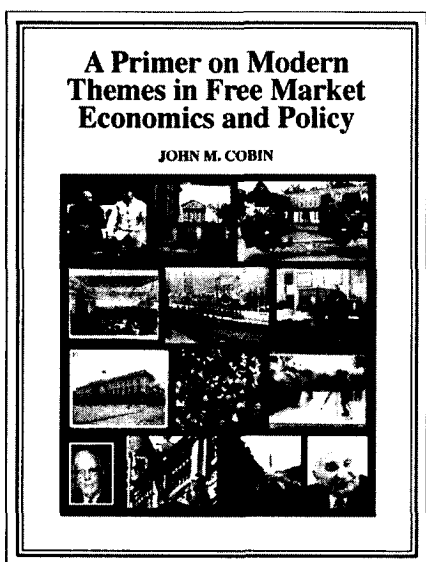
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26. William E. Rappard, *The Quest for Peace Yesterday and Today* (London: The David Davies Memorial Institute of International Studies, 1954).

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28. William E. Rappard, *The Secret of American Prosperity* (New York: Greenburg Publisher, 1955).

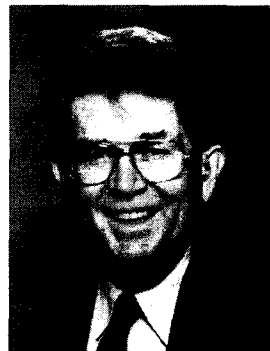


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Creating Jobs vs. Creating Wealth

Government policies are commonly evaluated in terms of how many jobs they create. Restricting imports is seen as a way to protect and create domestic jobs. Tax preferences and loopholes are commonly justified as ways of increasing employment in the favored activity. Presidents point with pride to the number of jobs created in the economy during their administrations. Supposedly the more jobs created the more successful the administration. There probably has never been a government spending program whose advocates failed to mention that it creates jobs. Even wars are seen as coming with the silver lining of job creation.

Now there is nothing wrong with job creation. Working in jobs is an important way people create wealth. So the emphasis on job creation is an understandable one. But it is easy for people to forget that creating more wealth is what we really want to accomplish, and jobs are merely a means to that end. When that elementary fact is forgotten, people are easily duped by arguments that elevate creation of jobs to an end in itself. While these arguments may sound plausible, they are used to support policies that destroy wealth rather than create it. I shall consider a few of the depressingly many examples in this column and the next.

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Creating Jobs Is Not the Problem

The purpose of all economic activity is to produce as much value as possible with the scarce resources (including human effort) available. But no matter how far we push back the limits of scarcity, those limits are never vanquished. Scarcity will forever prevent us from securing all the things we desire. There will always be jobs to do—far more than can ever be done. So creating jobs is not the problem. The problem is creating jobs in which people produce the most value. This is the point of the apocryphal story of an engineer who, while visiting China, came across a large crew of men building a dam with picks and shovels. When the engineer pointed out to the supervisor that the job could be completed in a few days, rather than many months, if the men were given motorized earthmoving equipment, the supervisor said that such equipment would destroy many jobs. “Oh,” the engineer responded, “I thought you were interested in building a dam. If it’s more jobs you want, why don’t you have your men use spoons instead of shovels.”

As I tell my students at the University of Georgia, I will employ every person in our college town of Athens if they’ll only work for me cheaply enough, say a nickel a month. Lower the wage a bit more and I’ll hire everyone in the entire state of Georgia. If I hired workers at those wages, I could make a profit having them build dams with spoons. Of course, the students recognize that my offer is

silly since they can make far more working for other employers, which reflects the more important reason my offer is silly—concentrating on the number of jobs ignores the value being created, or not created. More value will be produced in the higher-paying jobs my students can get than in the ones I am offering. A big advantage realized from the wages that emerge in open labor markets is that they attract people into not just any employment, but into their highest-valued employment.

Another advantage of market wages is that they force employers to consider the opportunity cost of hiring workers—their value in alternative jobs—and to remain constantly alert for ways to eliminate jobs by creating the same value with fewer workers. All economic progress results from being able to provide the same, or improved, goods and services with fewer workers, thus eliminating some jobs and freeing up labor to increase production in new, more productive jobs. The failure to understand this source of increasing prosperity explains the widespread sympathy with destructive public policies.

Dynamiting Our Way to More Jobs

In the 1840s a French politician seriously advocated blowing up the tracks at Bordeaux on the railroad from Paris to Spain to create more jobs in Bordeaux. Freight would have to be moved from one train to another and passengers would require hotels, all of which would mean more jobs. (This proposal was discussed and demolished by the nineteenth-century economist and essayist Frederic Bastiat in *Economic Sophisms*, pp. 94–95, available from FEE.)

This proposal is even more absurd than my offer to hire people for a nickel a month. At least I would employ workers to produce something of value, rather than to partially undo damage that is inflicted needlessly. Unfortunately, absurdity does not prevent economically destructive policies from being proposed and implemented. Using the job-creation justification, politicians commonly enact legislation that increases the effort required to produce a given amount of value.

One of the arguments for restricting imports is that it will create (or protect) domestic jobs. True, it will create some domestic jobs, just as destroying a section of a rail line will create domestic jobs. But also like a break in a rail line, import restrictions make it more costly to obtain valuable products. The only reason a country imports products is that it is the cheapest way to acquire them; it takes fewer workers to obtain the imported products through foreign trade than by producing them directly. In this way trade is like a technological advance, freeing up workers and allowing them to increase the production of goods and services available for consumption. Import restrictions create jobs in the same way dynamiting our railroads, bombing our factories, and requiring that workers use shovels instead of modern earth-moving equipment would create jobs. Always keep in mind that creating jobs is a means to the ultimate end of economic activity, which is creating wealth.

Creating Government Jobs

Because people tend to think of jobs as ends rather than means, they are easily fooled into supporting government programs on grounds that jobs will be created. We have all heard people argue in favor of military bases, highway construction, and environmental regulations on business on these grounds. To justify spending, government agencies commonly perform benefit/cost studies in which the jobs created are counted as benefits. This is like counting the hours you work to earn enough money to buy a car as one of the car's benefits. The jobs created by a government project represent a cost of the project: the opportunity cost. The workers employed in government activities could be producing value doing something else. The relevant question is not whether a government project creates jobs, but whether the workers in those jobs will create more wealth than they would in other jobs. This is a question advocates of government programs don't want asked. If it were, there would be far fewer low-productivity government jobs and far more high-productivity private-sector jobs. □

Nock on Education

by Wendy McElroy

The self-proclaimed “philosophical anarchist” Albert Jay Nock thought he was so superfluous to the society around him that he titled his 1943 autobiography *Memoirs of a Superfluous Man*. He felt utterly out of step with the twentieth century.

Born in 1870, he witnessed the severe societal changes resulting from world wars, revolutions in ideology, and the consequences of political measures passed decades earlier. He watched with particular concern as American schools abandoned classical education in favor of the less disciplined liberal arts approach favored by John Dewey and his followers. Nock charted what he saw as the disastrous consequences to American society of democratizing education. In doing so, he opposed one of the most popular trends of the early twentieth century: mass education.

Michael Wreszin, author of *The Superfluous Anarchist: Albert Jay Nock*, called popular education “the watchword of the progressive era” because “no other field of reform promised such grand possibilities.” The public school system was viewed as an invaluable means to reconstruct society by molding the generations to come. In his watershed book *Democracy and Education* (1916), Dewey wrote that popular education should be used as a conscious tool to remove social evil and promote social good. Slowly, the classical curricula aimed at rigorous education—

including, for example, Latin and a stress on history—were replaced by programs aimed at creating “good citizens.”

In the optimistic years before World War I, Nock enthusiastically embraced the “new education.” On seeing its application, however, he became one of Dewey’s earliest and staunchest critics. Nock’s later admirers attempted to revive classical education. Mortimer Adler, Stringfellow Barr, and Robert Maynard Hutchins translated their love of a classical curriculum into the Great Books program. But it was not until the 1950s, when the alleged superiority of Russian scientific knowledge and training became a national concern, that Americans seriously questioned whether public schools adequately educated their children.

Nock’s critiques of the American educational experiment ring fresh today because they offered fundamental objections to the underlying theories of popular education. He rejected, for example, educational egalitarianism. He saw no reason to believe that equal rights and treatment under the law implied that everyone had equal intellectual capacities any more than it implied that everyone would grow to the same height.

Yet he was careful to praise the intentions of parents who sent their children to public schools. In his book *Free Speech and Plain Language*, Nock wrote: “The representative American, whatever his faults, has been notably characterized by the wish that his children might do better by themselves than

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he could do by himself. . . . [I]n its essence and intention our system [of education] may be fairly called no less than an organization of this desire; and as such it can not be too much admired or too highly praised." Nevertheless, public schools were doomed to fail because "from beginning to end" they were "gauged to the run-of-mind American rather than to the picked American." They were designed to accommodate the lowest intellectual denominator, rather than the highest.

For his views on education, some commentators have called Nock an elitist. Be that as it may, the probing questions he asked about American education and its impact on the American character deserve to be explored and answered.

Nock: The Man

Albert Jay Nock was born in Scranton, Pennsylvania, to a respectable but poor family, which relocated a few years afterward to Brooklyn, New York. He learned to read without formal assistance by staring at a news clipping posted on his wall until, at the age of three, he could spell out words. The first book to catch his fancy was Webster's Dictionary, which he read for the sheer joy of learning language. His father was an Episcopal clergyman and thus no stranger to providing instruction, but he exercised only unobtrusive guidance over his son's self-education, which included mastery of Greek and Latin.

Eventually, Nock went to a private preparatory school in order to pass the entrance examinations for college. Of the private school, Nock stated that the students were never told not to put "beans up our noses, or subjected to any sniveling talk about being on our honour, or keeping up the credit of the dear old school, or any such odious balderdash. Nevertheless, we somehow managed to behave decently." In short, students were left alone to learn at their own pace, being given only the instruction they requested or clearly required.

At college—St. Stephen's, now Bard College—the same spirit of academic independence reigned. Nock wrote, "We were made to understand that the burden of education

was on us and no one else, least of all our instructors; they were not there to help us carry it or to praise our efforts, but to see that we shouldered it in proper style and got on with it." Being given the opportunity to pursue knowledge and then being left alone to do so remained Nock's ideal. Robert M. Crunden's biography, *The Mind and Art of Albert Jay Nock* (1964), contains the following anecdote:

Nock's friend, Edward Epstean, told him, "You've done a great deal for all those young people [who worked at Nock's magazine, *The Freeman*]."

"I don't know that I've ever done anything for them except leave them alone," Nock said.

"Yes, I understand," answered Epstean. "But if someone else had been letting them alone, it would have been a very different story."

Nock did some graduate work at Berkeley Divinity School in Connecticut, then decided in 1897 to be ordained as a minister of the Episcopal Church. After 12 years, he withdrew from preaching to join the staff of the *American Magazine*, where he stayed until 1914.

During this period, he developed a specific social philosophy. He became a single-taxer—a follower of the classical-liberal reformer Henry George—because he believed that private ownership of land led to monopoly and, in turn, a war between labor and capital. By abolishing all taxes save one on land, that war, as well as extremes of "unearned" wealth, could be avoided.*

As a pacifist, Nock opposed American entry into both world wars. As a radical individualist, he spoke out against collectivism and the policies of Franklin D. Roosevelt. Nock was deeply influenced by Franz Oppenheimer's masterpiece, *The State*—published in German in 1908, with an English translation in 1915. Oppenheimer argued that people achieved their goals, including basic survival,

*Editor's Note: See Murray Rothbard, *Man, Economy, and State*, Vol. II (Los Angeles: Nash Publishing Corporation, 1970 [1962]), pp. 512–13, 813–14.

either by economic means (work) or by political means (theft). Nock immediately adopted this distinction and used it as a touchstone in his social analysis. Although Nock was often called a liberal, he rejected the label, preferring to call himself a radical. To him, a liberal used the political means to improve and expand the State as a social institution. Nock proposed to eliminate the State from society. (He distinguished the State from the government.) His unswerving suspicion of the State—the political means—would be key to his approach to public education.

In 1920 Nock, along with the British classical liberal Francis Neilson, founded the individualist periodical *The Freeman*.^{*} By the time it closed in 1924, Nock had gained wide respect as an editor.

While teaching briefly at Bard College, Nock delivered what are known as the Page-Barbour lectures at the University of Virginia. There he roundly defended classical education against the theories of Dewey. The lectures were published in book form as *The Theory of Education in the United States* (1932). From February 1936 to September 1939 Nock wrote a series of monthly essays for the *American Mercury* titled “The State of the Union.” This series won him renown as a writer. (See Albert Jay Nock, *The State of the Union: Essays in Social Criticism*, ed. Charles H. Hamilton, 1991.)

Nock's Laws of Social Order

Before discussing the specifics of Nock's theories on education, it is useful to examine the more fundamental principles, or laws, with which he approached any social issue.

In *Free Speech and Plain Language*, Nock explained that “With regard to . . . all . . . aspects of our equalitarian social theory, my only aim is the humble one of suggesting that we bear in mind the disregard that nature has for unintelligent good intentions, and the vixenish severity with which she treats them.” He believed three laws defined social life—Epstein's law, Gresham's law, and the law of

diminishing returns—and he wanted people, particularly through government, to stop trying to thwart those “natural laws.”

Nock's first law of social order was named after his friend Edward E. Epstein from whom he first heard the principle. As rephrased in *Free Speech and Plain Language*, the law is, “Man tends to satisfy his needs and desires with the least possible exertion. Not, it must be understood, that he always does so satisfy them, for other considerations—principle, convention, fear, superstition or what not—may supervene; but he always tends to satisfy them with the least possible exertion, and, in the absence of a stronger motive, will always do so.” Nock applied this law to the political means. He believed that as long as the State could “confer an economic advantage at the mere touch of a button,” people would maneuver to “get at the button, because law-made property is acquired with less exertion than labour-made property.”

Nock's second law was adapted from Gresham's law on the nature of currency. Simply stated: bad money drives out good. When government dictates equivalency of value, the worst form of currency will circulate and the better money will disappear. Nock extended Gresham's law to cover culture. He asked the reader to imagine a concert being played for an audience of 300 randomly chosen people. He argued that the program would not include the best music produced through the centuries, but the most popular music of the moment. So too with education: bad education would drive out good. Mass education did nothing more than reduce the quality of education to what Nock called “the dreadful average.”

Nock's third law was based on the law of diminishing returns. He wrote that “The law of diminishing returns is fundamental to industry. It formulates the fact, which strikes one as curiously unnatural that, when a business has reached a certain point of development, returns begin to decrease, and they keep on decreasing as further development proceeds.” Consider the experience of vacationing at a location that has not yet been “discovered” by floods of tourists. When tourists begin to flock to the location, the return to

^{*}Editor's Note: That publication was not formally related to *The Freeman* that is the predecessor of *Ideas on Liberty*, which was founded later by admirers of Nock.

everyone abruptly decreases. In accommodating popular demands, the vacation site (like other things in life) falls prey to the law of diminishing returns.

For Nock, the third law contradicted a great myth of American education, namely, that "if a few qualified persons get this [educational] benefit, anybody, qualified or unqualified, may get it." But the "margin of diminishing returns" mandates that "the larger the proportion of unqualified persons" who attempt to receive the benefit, the swifter the benefits to all will vanish.

Education versus Training

In *The Theory of Education in the United States*, Nock claimed that American public schools were "based upon the assumption, popularly regarded as implicit in the doctrine of equality, that everybody is educable. This has been taken without question from the start." Nock questioned it. As noted, he did not believe that equal rights and equal treatment under the law held any implication for equal intellectual ability.

Nock made a crucial distinction between being "educable" and being "trainable." An educated person was one who had profited from absorbing "formative" knowledge. As a result, he had developed "the power of disinterested reflection"; that is, he could reason toward truth, unencumbered by emotional reactions or prejudice. Rather than aiming at a vocational goal, education aimed at the joy of ideas and produced men to whom learning was pleasure. A knowledge of Greek and Latin was particularly important, in Nock's view, because it allowed people to view the record of inquiring human minds for over 2,500 years.

In *On Doing the Right Thing and Other Essays*, Nock explained that education produced "intelligenz" [sic]—"the power invariably, in Plato's phrase, to see things as they are, to survey them and one's own relations to them with objective disinterestedness, and to apply one's consciousness to them simply and directly, letting it take its own way over them uncharted by prepossession, unchanneled by prejudice, and above all uncontrolled by rou-

tine and formula." The educated man was capable of independent thought. Unfortunately, Nock believed few people were educable.

By contrast, Nock thought most people could be trained. The trainable person profited from instrumental knowledge. In his essay "The Nature of Education," Nock explained that "When you want chemists, mechanics, engineers, bond-salesmen, lawyers, bankers and so on, you train them; training, in short, is for a vocational purpose. Education contemplates another kind of product." Nock did not mean to denigrate those who should be trained rather than educated. He wrote in his memoirs that "Education, properly applied to suitable material, produces something in a way of an Emerson; while training, properly applied to suitable material, produces something in the way of an Edison." Thus to Nock, science was a matter of training and many of the world's most eminent men were not educated but trained. "Training is excellent," he wrote in *Free Speech and Plain Language*, "and it can not be too well done, and opportunity for it can not be too cheap and abundant."

The main problem with the American educational system was that, in attempting to educate everyone equally, it encountered Gresham's law and ended up educating no one adequately. Instead, it provided only training, even to those who were educable. He believed that, in his era, "the study of history, like other formative studies, does not even rise to the dignity of being a waste of time. What with the political, economic and theological capital that has to be made of it . . . it is a positive detriment to mind and spirit." Indeed, he continued in *The Book of Journeyman* (1930), "Following the strange American dogma that all persons are educable, and following the equally fantastic popular estimate placed upon mere numbers, our whole educational system has watered down its requirements to something precious near the moron standard. The American curriculum in 'the liberal arts' is a combination of bargain-counter, grab-bag and Christmas-tree."

Nock's solution? The two categories of people should attend separate learning centers. As a blueprint, Nock praised Thomas Jefferson's scheme for public education. In *Free*

Speech and Plain Language, Nock wrote that “when Mr. Jefferson was revising the Virginia Statutes in 1797, he drew up a comprehensive plan for public education. Each ward should have a primary school for the R’s, open to all. Each year the best pupil in each school should be sent to the grade-school, of which there were to be twenty, conveniently situated in various parts of the state. They should be kept there one year or two years, according to results shown, and then all dismissed but one, who should be continued six years. . . . At the end of six years, the best ten out of the twenty were to be sent to college, and the rest turned adrift.”

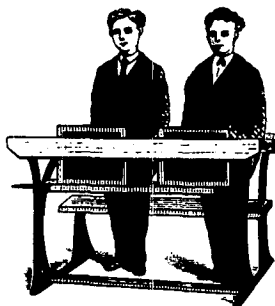
Unfortunately, Nock’s praise of Jefferson’s education scheme did not include a counterbalancing criticism of how this system was to be financed—namely, from the public trough. As an anarchist, Nock must have opposed a tax-supported school system, but his comments give the opposite impression. For example, of Jefferson’s scheme, he wrote, “As an expression of sound public policy, this plan has never been improved upon.”

As noted, dividing society into the “educable” and the “trainable” left Nock vulnerable to charges of elitism, especially when considered in conjunction with his theory of “the Remnant”—the select few of mankind on whom falls the burden of maintaining and advancing civilization. But his questions and insights cannot be dismissed lightly.

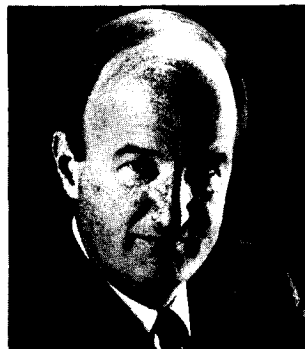
For example, sensitive to the difference between an individual and a citizen of a State, Nock believed that public schools were more interested in turning out good citizens than good individuals. For one thing, educated people were likely to question the political

system. He wrote that “Education . . . leads a person on to ask a great deal more from life . . . and it begets dissatisfaction with the rewards that life holds out. Training tends to satisfy him with very moderate and simple returns. A good income, a home and family, the usual run of comforts and conveniences, diversions addressed only to the competitive or sporting spirit or else to raw sensation—training not only makes directly for getting these, but also for an inert and comfortable contentment with them. Well, these are all that our present society has to offer, so it is undeniably the best thing all round to keep people satisfied with them, which training does, and not to inject a subversive influence, like education, into this easy complacency. Politicians understand this.” When you educate a man, you send him “out to shift for himself with a champagne appetite amidst a gin-guzzling society.”

In her introduction to Nock’s *Snoring as a Fine Art*, Suzanne La Follette paid tribute to her friend and colleague in terms that would have surely delighted him. She spoke of his unique talent for recognizing and encouraging ability in anyone he met. And she cautioned that his benevolence to those of ability was not “a conscious service to society or his country or even to the beneficiary. It was, I suppose, the teacher’s instinct in him; the instinct to serve truth. But he never tried to impose his truth on his pupil. Rather, he was concerned to put the pupil in the way to find truth for himself—as if he had revised the Biblical saying, ‘Ye shall know the truth, and the truth shall make you free,’ to read, ‘Ye shall be free in order that ye may know the truth.’” □



Economics for the 21st Century



“Nature has set no limit to the realization of our hopes.”

—MARQUIS DE CONDORCET

Recently I came across the extraordinary writings of the Marquis de Condorcet (1743–94), a mathematician with an amazing gift of prophecy in *l'age des lumières*. Robert Malthus (1766–1834) ridiculed Condorcet's optimism in his famous *Essay on Population* (1798). Today Malthus is well known and Condorcet is forgotten. Yet it is Condorcet who has proven to be far more prescient.

In an essay written over 200 years ago, translated as “The Future Progress of the Mind,” Condorcet foresaw the agricultural revolution, gigantic leaps in labor productivity, a reduced work week, the consumer society, a dramatic rise in the average life span, medical breakthroughs, cures for common diseases, and an explosion in the world's population.

Condorcet concluded his essay with a statement that accurately describes the two major forces of the twentieth century—the destructive force of war and crimes against humanity, and the creative force of global free-market capitalism. He wrote eloquently of “the errors, the crimes, the injustices which still pollute the earth,” while at the same time cel-

ebrating our being “emancipated from its shackles, released from the empire of fate and from that of the enemies of its progress, advancing with a firm and sure step along the path of truth, virtue and happiness!”¹

As we enter the year 2000, the public has focused on the history of the twentieth century. Condorcet's essay reflects two characteristics of this incredible period. First, the misery and vicious injustices of the past hundred years, and second, the incredible economic and technological advances during the same time.

The Crimes of the Twentieth Century

Paul Johnson's *Modern Times*, by far the best twentieth-century history of the world, demonstrates powerfully that this century has been the bloodiest of all world history.² Here is a breakdown of the carnage:

Civilians Killed by Governments (in millions)

Soviet Union	62 (1917–91)
China (communist)	35 (1949–)
Germany	21 (1933–45)
China (Kuomintang)	10 (1928–49)
Japan	6 (1936–45)
Other	36 (1900–)
Total.	170 million

Mark Skousen (<http://www.mskousen.com>; mskousen@aol.com) is an economist at Rollins College, Department of Economics, Winter Park, FL 32789, a Forbes columnist, and editor of *Forecasts & Strategies*. His textbook, *Economic Logic*, is now available from FEE.

Deaths in War (in millions)

International wars.	30
Civil wars.	7
Total.	37 million

Economists use a statistic to measure what national output could exist under conditions of full employment, called Potential GDP. Imagine the Potential GDP if the communists, Nazis, and other despots hadn't used government power to commit those hateful crimes against humanity.

Another great French writer, Frederic Bastiat (1801–50), wrote an essay in 1850 on “What Is Seen and What Is Not Seen.”³ We do not see the art, literature, inventions, music, books, charity, and good works of the millions who lost their lives in the Soviet gulags, Nazi concentration camps, and Pol Pot's killing fields.

The Economic Miracle of the Twentieth Century

Yet the twentieth century was also the best of times, for those who survived the wars and repression. Millions of Americans, Europeans, and Asians were emancipated from the drudgery of all-day work by miraculous technological advances in telecommunications, agriculture, transportation, energy, and medicine. The best book describing this economic miracle is Stanley Lebergott's *Pursuing Happiness: American Consumers in the Twentieth Century* (Princeton University Press, 1993). Focusing on trends in food, tobacco and alcohol, clothing, housing, fuel, housework, health, transportation, recreation, and religion, he demonstrates powerfully how “consumers have sought to make an uncertain and often cruel world into a pleasanter and more convenient place.” As a result, Americans have increased their standard of living at least tenfold in the past 100 years.

What should be the goal of the economist in the new millennium? Certainly not to repeat the blunders of the past. In the halls of Congress, the White House, and academia, we need to reject the brutality of Marxism, the weight of Keynesian big government, and the

debauchery of sound currency by interventionist central banks. Most important, ivory-tower economists need to concentrate more on applied economics (like the work of Lebergott) instead of high mathematical modeling.

As far as a positive program is concerned, the right direction can be found in an essay on the “next economics” written by the great Austrian-born management guru Peter F. Drucker almost 20 years ago: “Capital is the future . . . the Next Economics will have to be again micro-economic and centered on supply.” Drucker demanded an economic theory aiming at “optimizing productivity” that would benefit all workers and consumers.⁴ Interestingly, Drucker cited approvingly from the work of Robert Mundell, the newest Nobel Prize winner in economics, who is famed for his advocacy of supply-side economics and a gold-backed international currency.

Beware the Enemy

Market forces are on the march. The collapse of Soviet communism has, in the words of Milton Friedman, turned “creeping socialism” into “crumbling socialism.” But let us not be deluded. Bad policies, socialistic thinking, and class hatred die slowly. Unless we are vigilant, natural liberty and universal prosperity will be on the defensive once again.

We need to deregulate, privatize, cut taxes, open borders, stop inflating, balance the budget, and limit government to its proper constitutional authority. We need to teach, write, and speak out for economic liberalization as never before. Let our goal for the coming era be: freedom in our time for all peoples! □

1. Marquis de Condorcet, “The Future Progress of the Human Mind,” *The Portable Enlightenment Reader*, ed. Isaac Kramnick (Penguin Books, 1995), p. 38. Several of Condorcet's writings can be found in this excellent anthology.

2. Paul Johnson, *Modern Times: The World from the Twenties to the Nineties*, rev. ed. (New York: Harper, 1992). The best survey of the horrors of communism is *The Black Book of Communism: Crimes, Terror, Repression* (Cambridge, Mass.: Harvard University Press, 1999), written by six French scholars, some of whom are former communists.

3. Frederic Bastiat, *Selected Essays on Political Economy* (Irvington-on-Hudson, N.Y.: Foundation for Economic Education, 1995 [1964]).

4. Peter F. Drucker, *Toward the Next Economics, and Other Essays* (New York: Harper & Rowe, 1981), pp. 1–21.

CAPITAL LETTERS



Live by the Stats, Die by the Stats

To the Editor:

Regarding Mark Skousen's column, "Chicago Gun Show," in the October 1999 issue of *The Freeman: Ideas on Liberty* the statistical arguments advanced by the Chicago school allegedly demonstrating gun ownership reduces violent crime are methodologically flawed. Though I am a proud gun owner and lifetime NRA member, I believe citing these specious arguments is decidedly un-Austrian.

There are several reasons statistics are invalid proofs for explaining human action. First, they are descriptions of the past. Past behavior does not determine future behavior. Second, because the competing potential causal factors cannot be held constant, it is impossible to assign cause to effect. Mr. Lott's graph could also be used to show the drop in violent crime after the Brady Bill, which occurred at approximately the same time, by simply changing the caption at the bottom. Third, statistical samples are always incomplete, as was stated in the article. Even the U.S. census fails to account for 100 percent of the population. It is pure speculation as to how the missing part of the population would have affected the statistics gathered and the conclusions drawn. Last, statistics are always summaries of sample data, which is another way of saying they are incomplete explanations. For instance, an average only accurately explains a very small part of a sample.

The article ends with a specious conclusion: "All this confirms a long-standing constitutional principle: People have the right to own a gun for self-protection."

But statistical arguments cannot confirm the existence of a right! I have the right appropriately to use lethal force in self-defense regardless of its effect at deterring crime, for that matter regardless of the Constitution. The Second Amendment does not grant me the right to keep and bear arms; it recognizes that right and protects it. In this case, the statistical arguments offered can only impotently attempt to prove the effectiveness of gun ownership in deterring violent crime. And they can't even accomplish that for the reasons cited above. While I agree with the argument that criminal behavior must logically be deterred by the potential for self-defense, the means by which I arrive at that conclusion matter. The Austrian methodology—verbal logic—is the appropriate one. I'm surprised and slightly disappointed to see a specious Chicago school statistical argument finding its way into this esteemed Austrian school publication.

—TODD SHOENFELT
San Francisco

Mark Skousen replies:

True, you can't prove anything with statistics, but quantitative studies do provide evidence in support of basic economic principle. In the case of crime, John Lott provided strong evidence that when you raise the cost of committing a crime, fewer crimes are committed—essentially confirming the law of demand. Now you can use "verbal logic" till you're blue in the face in defense of the downward-sloping demand curve, but statistical evidence from the past can do wonders to liberate the mind from false notions (many of which exist in the controversial issue of gun control).

I grant you that sometimes data contradict a theory, but that does not mean that statistical work is never valuable. It simply means further analysis is necessary. But in no case should economists ignore statistical studies that contradict a hypothesis.

I should point out that many "Austrian" economists have used statistical evidence in

support of their position, including Murray Rothbard in *America's Great Depression* and Walter Block in his work *Economic Freedom of the World* (co-authored with James Gwartney and Robert Lawson). The latter work included a graph demonstrating that the higher a nation's level of economic freedom, the higher the per capita income. Such graphs have a far greater influence for good than mere "verbal logic."

Mental Illness a Myth?

To the Editor:

According to Thomas Szasz, the scientific criterion for disease is a "derangement in the structure or function of *cells, tissues and organs*" (*The Freeman: Ideas on Liberty*, November 1999). Based on this definition, he states that mental illnesses or brain disorders are not physical diseases because they can be neither detected nor diagnosed by examining cells, tissues, or organs.

But research over the past several decades shows that mental illnesses or brain disorders are in fact physical diseases. The brain is of course an organ. Brain disorders are caused by biochemical imbalances, i.e., derangements, in the brain's neurotransmitting systems.

However, mental illnesses or brain disorders are unique among physical diseases in that symptoms of this disease are primarily mental or behavioral rather than physical. Ideally, in the future, medicine will be able to look into the brain, analyze the malfunctioning of neurotransmitters such as serotonin or dopamine, diagnose the biochemical imbalance, and prescribe an appropriate medica-

tion. But the inability to do this at this time should not detract from the current scientific insight that mental illnesses or brain disorders are physical diseases that can be treated with medications the same as other physical diseases.

—JAMES A. WEBER
Chicago

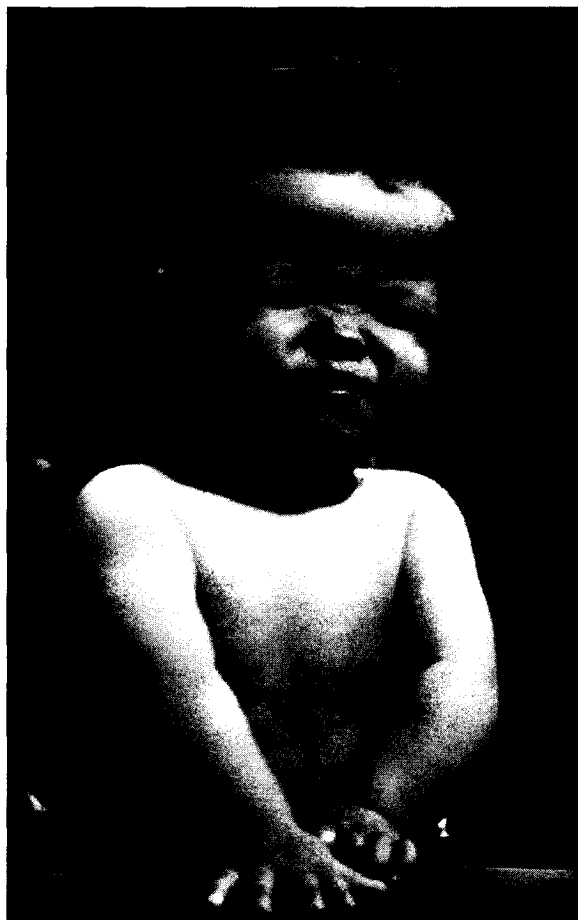
Thomas Szasz replies:

It is disheartening to read Mr. Weber's statement that I say "that mental illnesses or [sic] brain disorders are not physical diseases." I clearly stated that I do not consider "mental illnesses" to be synonymous with brain disorders, and that "[if] 'mental illness' means brain disease, then it is not a disease of the mind and psychiatry would be absorbed into neurology and disappear." The brain is an organ of the body; any process found to be a disease of the brain therefore lies within the province of neurology. The mind is not an organ of the body.

Mr. Weber also states: "However, mental illnesses or brain disorders are unique among physical diseases in that symptoms of this disease are primarily mental or behavioral rather than physical." This is erroneous. The initial symptoms of many bodily diseases may be primarily "mental" (fatigue, insomnia). The presence of bodily disease cannot be reliably inferred from symptoms or from response to "treatment," as Mr. Weber suggests. It is inferred from finding lesions. In "mental disease" there is no lesion; that is why, in psychiatry, diagnosis is mistaken for—and is accepted as—a disease.

We will print the most interesting and provocative letters we receive regarding articles in *Ideas on Liberty* and the issues they raise. Brevity is encouraged; longer letters may be edited because of space limitations. Address your letters to: *Ideas on Liberty*, FEE, 30 S. Broadway, Irvington-on-Hudson, NY 10533; e-mail: iol@fee.org; fax: 914-591-8910.

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BOOKS

The New Know-Nothings: The Political Foes of the Scientific Study of Human Nature

by Morton M. Hunt

Transaction Publishers • 1998 • 404 pages

• \$59.95 cloth; \$24.95 paperback

Reviewed by George C. Leef

Morton Hunt is one of those honest “liberals,” that is to say, someone who holds some statist beliefs, but is dedicated to freedom of inquiry and the marketplace of ideas. His book *The New Know-Nothings* explores an important phenomenon, namely, the use of political and other coercive means to obstruct research into and discussion of aspects of human nature. There are plenty of people who turn Jeffersonian tolerance on its head and say, “I disagree with what you say, and will do everything I can get away with to make you shut up.” The book is about them.

Hunt, a sociology professor at the State University of New York, Stony Brook, divides his book into three sections—attacks on inquiry from the left, attacks on inquiry from the right, and attacks from points in between. Readers of *Ideas on Liberty* will find the first and last most interesting.

The first part is the longest and most important. Hunt addresses what he rightly calls illiberal liberalism. He writes, “What is illiberal . . . is the effort of partisans of any position in the debate to stifle or prevent the expression of opinions by the other side and particularly to block or forbid the efforts of researchers whose possible findings they view with fear or revulsion.”

Consider, for example, the treatment accorded to Arthur Jensen, the emeritus professor of psychology at the University of California who concluded years ago that observed IQ differences among racial groups have a hereditary basis. That conclusion calls into question the statist/collectivist dogma that environment must explain all group

differences, and consequently the mild-mannered (but stubborn) Jensen has been subjected to the kind of abuse one would expect playground bullies to mete out to a weak, unpopular child. Hunt goes into detail about the numerous times Jensen has been shouted down, threatened with physical violence, subjected to actual violence, and had his appearances canceled because of bomb threats and mob action.

Hunt recounts many other similar unpleasant stories. Hans Eysenck has been roughed up and had his glasses smashed for daring to say that heredity plays a role in intelligence. “Fascists have no right to speak,” screamed his leftist tormentors. J. Philippe Rushton has been subjected to a campaign that might have been hatched by the Ku Klux Klan and threatened with loss of his professorship for publicizing his politically incorrect findings on heredity. Hunt also writes of the travails of those who have had the temerity to suggest that there might be a hereditary predisposition toward crime, that genetics explains some of the observed male-female differences in academic performances, and more. This section of the book is a good reminder that many leftists have no more use for the marketplace of ideas than they do for the marketplace of goods.

The last section of the book, “attacks from points in between,” also covers some interesting controversies, among them the attacks against individuals who question “repressed memory syndrome,” the animal rights movement, and the “thou shalt not speak ill of day care” crowd.

The least convincing part of Hunt’s book is the central section, detailing “attacks from the right.” We find here no violence, threats, or mob action. The author’s complaint is that “right-wing” politicians have occasionally succeeded in defunding federal research. Although he argues that some of those politicians were pursuing a “know-nothing” agenda, he admits that often the “rightist” opposition stems from a philosophical view that the government just doesn’t have any business in paying for nosy research. Correct, and an important point. There is a world of difference between using violence and intimidation

against people who say unpopular things and saying that the government shouldn't subsidize research.

Moreover, Hunt informs us of instances where, after political funding for research projects was shut off or denied, the researchers succeeded in obtaining financial support from private foundations. Still, he worries that we might not get enough research if government doesn't intervene. His defense of government funding falls flat on its face, however. Not all knowledge is worth what it costs to obtain, and the best way to filter out wasteful research is to ask people or institutions if they are willing to pay for it.

Overall, a readable, stimulating book with more hits than misses. ☐

George Leef is director of the Pope Center for Higher Education Policy at the John Locke Foundation and book review editor of Ideas on Liberty.

A New Deal for Social Security

by Peter Ferrara and Michael Tanner

Cato Institute • 1998 • 264 pages • \$19.95 cloth; \$10.95 paperback

Reviewed by John Attarian

In 1980 Peter Ferrara produced the path-breaking critique *Social Security: The Inherent Contradiction*. Now he and the Cato Institute's Michael Tanner ably update his exposition of Social Security's flaws and offer a thought-provoking solution.

Social Security is a federal "social insurance" program paying retirement, disability, and survivors' benefits from taxes levied on labor income. Its flaws are glaring, and the case for repeal is powerful. The authors provide a concise, if uneven and derivative, history of Social Security, followed by a thorough discussion of its problems.

The first problem is the looming bankruptcy. Because the huge "Baby Boom" generation is due to retire in the near future, the Social Security "trust funds" will be unable to pay full benefits after 2032 unless the government imposes crippling tax increases. Social

Security's defenders claim that raising taxes by just 2.2 percentage points will fix it. Ferrara and Tanner neatly dispatch this argument, pointing out that at best this postpones the date of "trust fund" exhaustion.

The second problem is that Social Security offers today's workers poor returns for their taxes. Using calculations of lifetime tax payments and projected benefits for two-earner couples, one-earner couples, and single people, the authors show that most of today's young workers will actually get *negative* returns. Despite short-term fluctuations, private capital markets perform much better.

Third, Social Security is unfair to the poor, minorities, and women. The poor depend on it more than wealthier Americans, yet tend to die sooner and hence receive less in benefits. Having lower life expectancies than whites, blacks are likewise disadvantaged, paying taxes all their adult lives but often getting little or no retirement benefits. Social Security gives women either 50 percent of their husbands' benefits or benefits based on their own employment, whichever is larger. The former usually is larger, meaning that many women get no return at all for the taxes they paid.

Social Security is also damaging to the economy. Its high payroll tax makes many Americans unable to save. Lost savings mean less money for investment and therefore slower economic growth. The payroll tax also discourages employment. Social Security is probably reducing Gross Domestic Product by 6 to 11 percent annually. Ferrara and Tanner argue that "Privatizing Social Security would reverse these effects and lead to increased economic growth and a better standard of living for all Americans."

Facing similar problems, other nations have been abandoning "social insurance." The authors survey privatization developments, from Chile's pioneering 1981 reform to more recent efforts in other Latin American countries, Britain, Australia, and China.

Any reform, Ferrara and Tanner argue, should "irrevocably commit and emphasize" that benefits for current retirees would not be changed. It should also give payroll tax relief, provide a government-guaranteed

minimum benefit, and give private retirement accounts the same tax treatment as Individual Retirement Accounts. They propose letting workers create their own accounts, financing them with 10 percentage points of the current payroll tax and using the remaining 2.4 percentage points to pay current benefits. Workers choosing the private option would receive government "recognition bonds" to compensate for past Social Security taxes. At retirement, workers could buy annuities with their account money, make withdrawals, or both.

Critics of privatization argue that workers would have to finance simultaneously their own retirement and benefits for current retirees. The authors deny this, and devote many pages to explaining the financing of the transition. Possibilities include continued payroll taxes, the sale of federal assets, and reducing other federal spending. They also expect new revenue from taxes on the returns to the new investment. Economist Martin Feldstein estimates the real, pretax average rate of return on capital at 9.3 percent. Taxing three percentage points at the business level (before payment of interest and dividends), the authors argue, would generate abundant revenue to defray transition costs and still leave workers with much higher returns than Social Security offers.

Their proposal has *prima facie* appeal. However, they assume that the historical real rate of return on capital will continue to be realized, without making a case for it. And they seem to have forgotten that Feldstein estimates that federal, state, and local governments are *already* taxing capital at the business level at the rate of 3.9 percent. When we add the proposed 3 percent tax, we get a total tax rate of 6.9 percent, which leaves an after-tax rate of return for workers of just 2.4 percent (9.3 percent rate of return minus 6.9 percent taxes), not 6.3 percent. Finally, they retain the compulsory payroll tax. If Social Security is so awful, why keep one of its central features? Better to repeal the Social Security law and ditch this punishing tax.

Still, the book superbly illuminates the flaws in Social Security. The plan Ferrara and Tanner propose might not be ideal, but it

offers a welcome exercise in thinking the issues through. □

John Attarian is a freelance writer in Ann Arbor, Michigan, and adjunct scholar with the Mackinac Center for Public Policy. He has recently completed a book on Social Security.

Myths of Rich and Poor: Why We're Better Off Than We Think

by W. Michael Cox and Richard Alm

Basic Books • 1999 • 256 pages + xvi • \$25.00

Reviewed by Donald J. Boudreaux

I vividly recall a 1972 visit to the Sears store in our local mall. I was 14 years old and had never before seen an electronic calculator. But there at Sears, for the first time in my life, was this wonder to behold! Three different models were displayed beneath plexiglass cut so that the keyboards could be operated by shoppers—but also so that no one would steal this valuable inventory.

My parents had difficulty dragging me away from these magical machines—so magical that the high-end models could even calculate square roots! Unfortunately, I couldn't afford one. The cheapest model was priced at nearly \$100. "Oh well," I sighed. "In ten years when I have an adult job and a credit card, I'll buy one."

I'm sure that if a visitor from 1999 had then swooped down to inform me that in just a few years these technological marvels would cost no more than a movie ticket, I would have howled derisively. W. Michael Cox and Richard Alm aren't visitors from the future; instead, they're researchers of today who do fascinating and pioneering research on the progress of American living standards. They find, in a nutshell, that the affordability of nearly every good or service you care to name has risen over the years and continues to rise.

This finding contradicts the conventional wisdom spewed out daily by popular commentators. A favorite refrain is that the typical American today enjoys living standards that are no higher than those in 1973. The implication is that the market has sputtered for a quarter century.

Of course, personal observation over these years should be sufficient to convince most people of the absurdity of the “myth of ’73.” Anyone born before 1960 can easily list dozens of marvelous goods and services that today are commonplace, but which were unavailable to ordinary Americans (or anyone else) 25 years ago. Here’s my (very) partial list: personal computers, online bookstores, cell phones, quality disposable diapers, automobiles that almost never need tune-ups, and Jiffy Lube.

But there’s no need to rely on personal anecdotes and observations now that the data-rich research of Cox and Alm has been collected in *Myths of Rich and Poor*. Cox, the chief economist at the Federal Reserve Bank of Dallas, and Alm, a reporter for the *Dallas Morning News*, use readily available data to directly confront and blow the “myth of ’73” to smithereens.

Cox and Alm calculate how long the typical American worker of the past had to work to acquire various goods and services versus the amount of time required of the typical American worker of today. This calculation is far more revealing than the more standard calculations drawn from data on wages or household incomes, for the Cox-Alm calculation measures *directly* what ordinary Americans are able to consume. (Wages and income are affected by inflation; the size of the average household has shrunk over time; and increasing amounts of compensation come as fringe benefits—all of which make changes in wages and income relatively poor measures of changes in living standards.)

The Cox-Alm findings are stunning. From milk and assorted grocery items to televisions and other home electronics to gasoline, automobiles, and housing, the time the typical American must work to acquire any of those items is today significantly less than it was 25 years ago.

This increasing affordability, of course, translates into greater material comfort for almost all Americans. Table 1.2 in the book is one of the most illuminating collections of numbers I’ve ever seen. It shows that *poor* Americans today are more likely to own almost all household conveniences than were

typical middle-class Americans of a generation ago. For example, in 1971 about 83 percent of *all* American homes had a refrigerator. In 1994, nearly 98 percent of *poor* households owned one. The same general pattern holds for washing machines, clothes dryers, automatic dishwashers, stoves, microwaves, color televisions, air conditioners, and several other familiar items. So much for the canard that today’s prosperity is built on the backs of the poor.

While this is a superb book, it isn’t without some minor flaws. One is the authors’ claim that World War II “shook the country out of the decade-long Great Depression.” This is a curious claim coming from scholars who rightly emphasize that an economy’s performance is best measured by what its people can consume. Wartime production did not ease the lives of average Americans. Robert Higgs’s pioneering research shows that while the war years increased employment and military output, the Depression didn’t end until late 1946.

An even more curious claim by Cox and Alm is that “government can bolster competition through antitrust laws.” Not so. More than a century of antitrust regulation in the United States has provided ample evidence that such regulation is far more likely to stymie competition—by being targeted at especially entrepreneurial and successful firms—rather than bolster it. History also teaches that the market itself is extraordinarily adept at ensuring that, except for firms protected from competition by government, no company succeeds while behaving monopolistically.

The market’s ability to keep private firms from gaining harmful monopoly power should be evident to Cox and Alm, who explicitly (and properly) build their analyses upon the insights of Joseph Schumpeter. In his 1942 book *Capitalism, Socialism, and Democracy*, Schumpeter penned what remains today the finest explanation of the capitalist competitive process. Schumpeter understood that “pure cases of long-run monopoly must be of the rarest occurrence . . . unless buttressed by public authority.” Indeed. There’s no need to empower bureau-

crats to parade around pretending to keep markets competitive.

My complaints with this book are minor. *Myths of Rich and Poor* is a major accomplishment. Buy a copy and learn how remarkably productive a free society is. □

Donald Boudreaux is president of FEE.

The Letters of Centinel: Attacks on the U.S. Constitution, 1787–1788

by Samuel Bryan

edited and introduced by Warren Hope

Fifth Season Press • 1998 • 160 pages •

\$19.99 paperback

Reviewed by Richard M. Gamble

Understanding the Antifederalist complaint against the Constitution requires a sympathetic ear and an active historical imagination. It is not easy for a generation taught to revere the Constitution as holy writ to recognize what the Antifederalists feared in the form and powers of the new government proposed by the Philadelphia convention. Where today we see a model document praiseworthy for well-defined constraints, precise separation of powers, carefully balanced interests, and wise checks on political ambition, the Antifederalists saw a conspiracy to rob the American people of the liberties recently preserved by them in their war against Britain. Assuming telling pseudonyms like “Brutus” and “Cassius,” the Antifederalists campaigned relentlessly against what they saw as a diabolical plot to build an empire, a plot as bold and dangerous as Julius Caesar’s bid to overthrow the ancient Roman Republic.

Among the lesser-known Antifederalists was “Centinel,” the pen name of the eloquent and contentious Pennsylvania patriot Samuel Bryan. In step with Antifederalist themes, he blasted the new frame of government as a conspiracy of the “well-born few” to enslave the many, a stealthy and calculated attempt to found a despotic empire by means of unwarranted innovations in government, contrary to the history, habits, and senti-

ments of the American people. A handy compilation of Centinel’s trenchant critique of the Constitution is now available thanks to Warren Hope, who has edited and annotated 24 brief topical letters that appeared in Pennsylvania newspapers during and just after the ratification debate in 1787 and 1788. While the quality of these essays is uneven, the content redundant, and the tone at times shrill, the best of them brilliantly answer Publius’s more famous pro-ratification arguments in *The Federalist Papers*. Centinel’s warnings are arresting and prophetic.

Centinel’s objections to the Constitution and his predictions for the future of the Republic stand up well, especially in contrast to Hamilton’s comical reassurances in *The Federalist Papers* that the new government would be a model of restraint, modesty, and frugality. Subsequent experience with Leviathan has proven Centinel and his fellow Antifederalists correct on a number of counts. He warned with penetrating foresight about the very features of the Constitution that we have come to regret by sad experience: the ambiguous “necessary and proper” and “general welfare” clauses as windows to limitless federal power; the imperial tendencies of a standing army; the bottomless pit that the federal Congress’s power of taxation has become; and, above all, the “melting down” of the state legislatures and courts into meaningless and redundant entities, hopelessly inadequate bulwarks against national encroachment and consolidation.

Moreover, Centinel’s essays help puncture two enduring myths about the Antifederalists: first, that they opposed the Constitution *in toto* and without offering a reasonable alternative, and second, that they were reckless political radicals who loved liberty to the point of anarchy. Throughout his letters, Centinel conceded the need for a more “energetic” general government, including a solution to the nagging problems of taxation and a hobbled Congress. He denied that the choice was between *this* constitution and *no* constitution, between the order, prosperity, peace, security, and happiness promised by the Federalists and the anarchy, poverty, fragmentation, international humiliation, and misery

allegedly certain if the Antifederalists had their way.

Centinel asked for time to debate, revise, and "correct" the Constitution, not to destroy it. His central concern was that once lost, liberty would never be regained, and once gained, power would never be relinquished.

Far from a lover of anarchy, Centinel sought a modest and frugal government that suited the disposition of the American people. He praised tradition, experience, and America's rootedness in the common law; he warned of the "lust of dominion" that lay at the heart of human nature and human history; and he appealed to the authority of Blackstone and Montesquieu to expose the proposed Constitution's flaws. In his mind, the Federalists were the true innovators who would unsettle the habits of the people. Sounding like the patriots of two decades before, Centinel renewed the fight to defend inherited English rights from the encroachments of a remote and despotic government. He was determined to preserve the liberties that Pennsylvanians already enjoyed under their state constitution. In short, he believed he was trying to prevent a revolution in government.

Centinel was on the losing side of American history, but his essays force the modern reader to confront uncomfortable questions about the meaning of the founding. Did the Constitution preserve the name and form of the Republic while subverting its character? Did the design of the Constitution itself slowly but inexorably transform the United States into the bloated empire that Centinel predicted? Was the Constitution of 1787, even with the addition of a Bill of Rights, fatally flawed? The Antifederalists would not be the least surprised by the vastly changed condition of the United States two centuries later. □

Richard Gamble is professor of history at Palm Beach Atlantic College.



Foundations of Economics: Beginner's Companion

by Yanis Varoufakis

Routledge • 1998 • 396 pages • \$100.00 cloth;
\$32.99 paperback

Reviewed by Paul Heyne

This is an angry book. The administration of the University of Sydney, Australia, where Varoufakis is a senior lecturer in economics, did something in 1997 that "with a stroke of brilliance destroyed the atmosphere of collegiality and public spiritedness" that had previously characterized efforts to make the introductory economics course "a decent educational experience for the students." The administration thereby released Varoufakis, he writes, "from any moral imperatives, namely teaching introductory economics passionately," and led him to turn this book "into a kind of a testimonial."

The author never discloses exactly what the University of Sydney did. But if he and his colleagues were introducing undergraduates to economics in the manner that this book recommends and exemplifies, I know what it ought to have done: It should have told them to choose between teaching introductory economics in a reasonable way or turning the course over to someone who would.

Varoufakis does not disclose whether he was required to teach general equilibrium theory in the introductory course or whether he (and his colleagues) decided on their own that general equilibrium theory was the best form in which to present it. And there is another possibility. Disliking standard economic theory intensely, they decided to teach it in a form that was most likely to repel college students encountering economics for the first time.

The author tells us that the book was designed to complement conventional introductory economics textbooks and to relieve the "monotony and austerity" that is usually associated with them. If Varoufakis is a charismatic teacher, he may be able to teach this book along with a standard text without inciting a student rebellion. However, for anyone who is not both charismatic and thor-

oughly committed to the author's views on (1) the nature of economic theory, (2) the history of economics, (3) the insightful and illuminating character of very simple Marxian economic analysis, (4) the ideological nature of all social thought, and (5) the impossibility of testing any theory with reference to facts, I would counsel strongly against the attempt. No sensible economist who reads this book would assign it for an introductory course.

My comments will be directed to the first, third, and last of the views just listed. I have spent a little time in Australian universities and suspect that academic economists in Australia try harder than economists anywhere else to make the undergraduate degree a professional degree. But even they, so far as I know, don't begin with formal general equilibrium theory and all the unrealizable conditions it assumes.

There are versions of introductory economics that owe more to F. A. Hayek, Ronald Coase, and Douglass North than to general equilibrium advocates like Leon Walras and Gerard Debreu. Whatever might be true of advanced economic theory texts, introductory ones do not have to be "monotonous and austere." Textbooks modeled after the pioneering efforts of Armen Alchian and William Allen induce more students to go on to advanced work in economics than do books that confine themselves to technicalities remote from the students' experience and without application to the issues of the day.

The Marxian perspective Varoufakis prefers to the "austere" theory he first presents is one that has the capitalist appropriating all the surplus value produced by the laborer and thereby causing every economic ill from business cycles through decreasing real wages and the stifling of economic progress. His Marxian outlook renders him oblivious to anything that has happened in the twentieth century except perhaps the Great Depression. But Varoufakis, because he does not believe that theories can be either confirmed or refuted by facts, allows himself to make sweeping assertions about what's wrong with the world and what must be done to repair it on the basis of a theory that is far more melodramatic than plausible.

Varoufakis quotes none other than Ludwig von Mises in support of his claim that we cannot use facts to test economic theories. Mises maintained that the basic theorems of economics were a priori truths, not derived from experience and therefore incapable of empirical refutation. Whether or not one agrees with that position, Mises was decidedly not saying that the basic theorems of economics are arbitrary assertions grounded on nothing more than the political or ethical preferences of the economist. It is frightening to encounter people who, like Varoufakis, assert that there is no truth (which Mises never claimed), while vehemently demanding radical changes in long-established institutions.

Recall that the author intended this book as a testimonial. Its publication is an unintended testimonial—to the fact that a significant number of economists are still unaware of all that has gone on in economics in the past quarter century to transform the mainstream from a "monotonous and austere" collection of theorems to a powerful framework for understanding society. □

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Limited Government, Individual Liberty and the Rule of Law: Selected Works of Arthur Asher Shenfield

edited by Norman Barry

Edward Elgar Publishing • 1998 • 378 pages
• \$100.00

Reviewed by William H. Peterson

How well I remember Arthur Shenfield (1909–1990), an unforgettable man learned in law and economics and a keen student of a free society. We used to debate privately about who was the greater economist, Mises or Hayek. I chose Mises, he Hayek. I had the good fortune to hear Shenfield lecture, usually without notes, at the Philadelphia Society and the Mont Pelerin Society (where he served a term as president).

And what a lecturer! Those lectures—most are captured in articles reprinted in this

insightful book—were impeccable, perceptive, witty, rich in history and philosophy.

Shenfield recognized the stark fact of scarcity and the need for sound economics and the rule of law to cope with it. He saw capitalism as the way to generate widespread social cooperation as well as engage each individual's pursuit of happiness. No easy trick, but it is done, if hardly infallibly, daily around the globe.

Shenfield thus saw capitalism as a system driven not just by competition but also, again hardly infallibly, by moral principles such as trust, honesty, equal rights, and personal responsibility—including responsibility for charitable acts.

Shenfield was enthralled by Adam Smith's concept of the invisible hand by which self-interest, under the rule of law, translates into the public interest, which is to say, into rising living standards for the sovereign consumer. As for competition, he found himself at odds with the early Chicago school, especially with the late George Stigler and his long-time embrace of the Sherman Antitrust Act of 1890 as a means of precluding monopoly, collusion, cartels, and predatory pricing. Shenfield confesses that at first he embraced the Sherman Act for its supposed protection of competition, but was won over by the arguments of Mises and Hayek. They led him to conclude that the natural corrective forces of the marketplace are far superior to bureaucratic agencies, such as the Justice Department's Antitrust Division, which seek to bully competitors into behaving as the regulators think they should. In his excellent treatment of antitrust, Shenfield quotes fellow Mont Pelerin member Henri Lepage of France: "Let us not kill competition in the name of competition." Certainly Shenfield would have opposed the federal government's competition-numbing case against Microsoft.

Another important issue Shenfield raises is the so-called "third way" embraced by President Bill Clinton, British Prime Minister Tony Blair, and numerous intellectuals. The third way attempts to meld the best of capitalism with the best of socialism. Shenfield forcefully attacks this perennial delusion. The trouble

with the concept of "the best of socialism," Shenfield argues, is that there is no "best"; it is an illusion, a will-o'-the-wisp that socialists sell to a gullible public with emotional, envy-laden arguments that capitalism is based on selfishness, domination, and income inequality. Socialists foretell disaster if atomistic individualism is allowed free play without the cement of "social justice" to hold society together and if private property, especially "undemocratic" ownership of the tools of production, is not controlled by the state.

Shenfield and his wife (Dame Barbara Shenfield) spent much time in Sweden investigating the truth about the third way. His findings are reported in these pages. He maintains that the ruling Swedish intelligentsia is guilty of what Hayek called "the fatal conceit" for its encouragement of a virtually complete welfare state.

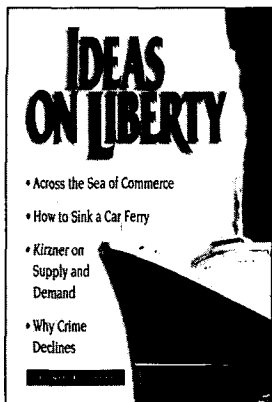
Not only was the third way economically ruinous, but Shenfield also indicted welfarism for inducing social breakdown. He cites approvingly Nobel economist Gunnar Myrdal's surprisingly honest description of his countrymen as reduced by welfarism to "hustlers and criminals." Crime rates for robbery, burglary, prostitution, street violence, car theft, drug trafficking, public drunkenness, and welfare fraud are on the rise. Suicide has also increased, most notably among younger people bored with life in the welfare paradise. Concludes Arthur Shenfield: "The true cause of Sweden's failure is socialism itself."

There is far more wisdom on a broad array of subjects to be found in this book than a review can possibly do justice to. Shenfield's writings will prove to be worthwhile reading for anyone who is a friend of liberty. □

William Peterson is an adjunct scholar at the Heritage Foundation in Washington and Distinguished Lundy Professor Emeritus in Business Philosophy at Campbell University in North Carolina.



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Capitalism and the Common Man



There are some arguments, having a faint measure of plausibility, that have served politicians, charlatans, and assorted do-gooders for well over a century in their quest for control. One of those arguments is: capitalism primarily benefits the rich and not the common man. That vision prompts declarations such as Representative Richard Gephardt's assertion that high-income earners are "winners" in "the lottery of life." Then there's Robert Reich, former secretary of labor, who calls high-income earners the "fortunate fifth." This nonsensical vision leads to calls for those who've been "blessed" to "give back" either voluntarily or coercively through the tax code.

While demagogic statements like these have high emotive worth, they reflect resolute, nearly incurable stupidity about the sources of income. Listening to some of the talk about income differences, one would think that out there somewhere is a pile of money. People who are wealthy just happened to get there first and greedily took an unfair share. Justice requires that they give back. Or there's talk about unequal income distribution. The way some people talk, you'd think there's a dealer of dollars who shells out \$1,000 to one person, \$100,000 to another, and a million dollars to yet another. Thus the reason why some people are wealthy while others are not

wealthy is that the dollar dealer is a racist, sexist, or multi-nationalist—or just plain mean. Economic justice requires a redealing of the dollars, income redistribution, where the ill-gotten gains of the few are returned to their rightful owners.

In a free society, for the most part, people with high incomes have demonstrated extraordinary ability to produce valuable services for, and therefore to please, their fellow man. Sam Walton, founder of Wal-Mart; Bill Gates, founder of Microsoft; and singer Michael Jackson provided services deemed highly valuable by their fellow men who voluntarily took money out of their pockets to purchase those services. Their high incomes stand as unambiguous proof of that service. Their high incomes also reflect the "democracy" of the marketplace. For example, millions upon millions of independent decision-makers decided to fork over \$200 for Gates's Windows 98 operating system. Those who think Gates is too rich and want to redistribute his income are really registering disagreement with the "democracy" of the marketplace and want to cancel or offset the market "vote."

Indeed, we might consider the dollars people earn as certificates of performance. Think of it in the following way. You hire me to mow your lawn. After I have completed the task, you give me \$20. I go to the grocer and demand a pound of steak and a six-pack of beer that my fellow man produced. The grocer says, "You're demanding something that your fellow man has produced. What have you done to serve him?" I reply, "I have served my

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fellow man by mowing his lawn.” The grocer says, “Prove it!” That’s when I hand him my \$20, my certificate of performance.

Income earners owe nothing else to their fellow man; they have met their social obligations. If “giving something back” means anything, it should be the admonition to thieves and social parasites: people who have taken and given nothing in return. We have it backwards. Highly productive (rich) people like Walton and Gates are held up to social ridicule, while thieves and bums are shown compassion and concern and have become society’s mascots.

Good for the Masses

Capitalism is the best thing that ever happened to the common man. The rich have always had access to entertainment, often in the comfort of their palaces and mansions. The rich have never had to experience the drudgery of beating out carpets, ironing their clothing, or slaving over a hot stove all day to have a decent dinner; they could afford to hire people. Capitalism’s mass production and marketing have made radios and televisions, vacuum cleaners, wash-and-wear clothing, and microwave ovens available and well within the means of the common man, sparing him the boredom and drudgery of the past. Today the common man has the power to enjoy more than what only the rich had yesteryear.

What about those who became wealthy making comforts available to the common man? Henry Ford benefited immensely from mass-producing automobiles, but the benefit for the common man from being able to buy a car dwarfs anything Ford received. Individuals and companies that produced penicillin and polio and typhoid vaccines may have become very wealthy, but again it was the common man who was the major beneficiary. In more recent times, computers and software products have benefited our health, safety, and quality of life in ways that far outstrip whatever wealth was received by their creators.

Here’s a little test. Stand on the corner and watch people walk or drive by. Then, based

on their appearances, identify which persons are wealthy. Years ago, that wouldn’t have been a difficult challenge. Ordinary people wouldn’t be dressed as well, surely not wearing designer clothing, nor would they have nice-looking jewelry. They wouldn’t be driving by. Compare the income status of today’s airline passengers with those of a few years ago and you’ll find a much greater percentage of ordinary people.

That’s one of the great benefits of capitalism; it has made it possible for common people to enjoy at least some of what wealthy people enjoy. One might assert that common people don’t have access to Rolls Royces and yachts. You’re wrong. Gates is super-rich and can afford to ride in a Rolls Royce and go yachting; but so can the common man—just not as long. He can rent a Rolls or a yacht for a day, a half-day, or an hour.

Capitalism is relatively new in human history. Before the rise of capitalism, the way people amassed great wealth was by looting, plundering, and enslaving their fellow man. Capitalism made it possible to become wealthy by serving one’s fellow man. Capitalists seek to discover what people want and then produce and market it as efficiently as possible.

Here’s a question that we should ponder: are the wealthy people who have created unprecedented convenience, longer life expectancy, and more fun for the ordinary person deserving of all the scorn and ridicule heaped on them by intellectuals and politicians? Are the wealthy really obliged to “give something back”? Exactly what more do the wealthy discoverers and producers of, say, life-saving antibiotics owe us? They’ve already saved lives and made us healthier.

Despite the miracles of capitalism, it doesn’t do well in popularity polls. One reason is that capitalism is always evaluated against the nonexistent, unrealizable utopias of socialism or communism. Any earthly system will pale in comparison to a utopia. But for the ordinary person, capitalism, with all of its warts, is superior to any system yet devised to deal with our everyday needs and desires. □

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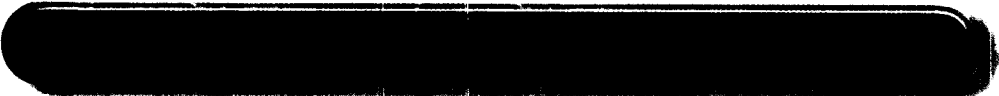
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